Form

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t;font-size:8pt;">16,179

$
7,679

$
8,100

$
6,670

Per Share Data[1]:

Net Income for Basic Earnings per Share
$
6,908

$
16,179

$
7,679

$
8,100

$

6,670

Basic Earnings per Share
$
0.40

$
1.01

$
0.55

$
0.64

$
0.56

Basic Weighted Average Shares Outstanding
17,338,348

15,962,902

14,014,219

12,628,676

11,990,757

Net Income for Diluted Earnings per Share
$
40,064

$
39,600

$
33,809

$
35,685

$
30,317

Diluted Earnings per Share[2]
$
0.40

$
0.58

$
0.50

$
0.53

$
0.45

Diluted Weighted Average Shares Outstanding
70,934,362

68,849,172

68,126,786

67,797,524

66,759,840

Cash Dividends Declared Per Share
$
0.37

$
0.41

$
0.41

$
0.35

$
0.25

1 The operating company issues shares of Class A common stock and Class B units that have non-forfeitable dividend rights. Under the “two-class method,” these shares and units are considered participating securities and are required to be included in the computation of basic and diluted earnings per share.

2 During the year-ended December 31, 2017, the calculation of diluted earnings per share resulted in an increase in earnings per share. Therefore, diluted earnings per share is assumed to be equal to basic earnings per share. See Note 5 to our consolidated financial statements beginning on page F-22 of this Annual Report for further details.

	As of December 31,				
	2017	2016	2015	2014	2013
	(in thousands)				
Statements of Financial Condition Data:					
Cash	$63,414	$43,522	$35,417	$39,109	$33,878
TOTAL ASSETS	169,047	179,121	114,309	111,886	80,213
TOTAL LIABILITIES	69,758	97,787	28,847	26,853	21,664
Non-Controlling Interests	66,985	52,841	67,040	66,632	42,187
EQUITY	32,304	28,493	18,422	18,401	16,362

TABLE OF CONTENTS

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

We are an investment management firm that utilizes a classic value investment approach across all of our investment strategies. We currently manage assets in a variety of value-oriented investment strategies across a wide range of market capitalizations in both U.S. and non-U.S. capital markets. At December 31, 2017, our assets under management, or AUM, was approximately $38.5 billion. We manage separate accounts on behalf of institutions, act as sub-investment adviser for a variety of SEC-registered mutual funds and non-U.S. funds, and act as investment adviser for the Pzena mutual funds, certain private placement funds and non-U.S. funds.

We function as the sole managing member of our operating company, Pzena Investment Management, LLC (the “operating company”). As a result, we: (i) consolidate the financial results of our operating company with our own, and reflect the membership interest in it that we do not own as a non-controlling interest in our consolidated financial statements; and (ii) recognize income generated from our economic interest in our operating company’s net income. As of December 31, 2017, the holders of our Class A common stock and the holders of Class B units of our operating company held approximately 26.3% and 73.7%, respectively, of the economic interests in the operations of our business.

The Company also serves as the general partner of Pzena Investment Management, LP, a partnership formed with the objective of aggregating employee ownership in one entity.

Certain of our named executive officers and employees have interests in Pzena Investment Management, LP and certain estate planning vehicles through which they indirectly own Class B units of our operating company. As of December 31, 2017, through direct and indirect interests, our five named executive officers; 38 other employee members; and certain other members of our operating company, including one of our directors, his related entities, and certain former employees, collectively held 49.4%, 4.7%, and 19.6% of the economic interests in our operating company, respectively.

Net Income

GAAP diluted net income and GAAP diluted earnings per share were $40.1 million and $0.40, respectively, for the year ended December 31, 2017, $39.6 million and $0.58, respectively, for the year ended December 31, 2016, and $33.8 million and $0.50, respectively, for the year ended December 31, 2015. During the year-ended December 31, 2017, the calculation of diluted earnings per share resulted in an increase in earnings per share. Therefore, diluted earnings per share is assumed to be equal to basic earnings per share.

In evaluating the results of operations, we also review non-GAAP measures of earnings, which are adjusted to exclude changes in the deferred tax asset and corresponding liability to the Company's selling and converting shareholders associated with a change in the calculation of historical 754 step-ups, the release of the valuation allowance in the fourth quarter of 2016, the impact of the Tax Cuts and Jobs Act enacted in the fourth quarter of 2017, as well as certain non-recurring charges recognized in operating expenses during 2015. We believe that these GAAP adjustments add a measure of non-operational complexity that partially obscures a clear understanding of the underlying performance of our business. We use these non-GAAP measures to assess the strength of the underlying operations of the business. We believe that these adjustments, and the non-GAAP measures derived from them, provide information to better analyze our operations between periods, and over time. Investors should consider these non-GAAP measures in addition to, and not as a substitute for, financial measures prepared in accordance with GAAP.

As adjusted, non-GAAP diluted net income and non-GAAP diluted earnings per share were $44.7 million and $0.63, respectively, for the year ended December 31, 2017, and $31.4 million and $0.46, respectively, for the year ended December 31, 2016, $34.5 million and $0.51, respectively, for the year ended December 31, 2015. GAAP and non-GAAP net income for diluted earnings per share generally assumes all operating company membership units are converted into Company stock at the beginning of the reporting period, and the resulting change to our GAAP and non-GAAP net income associated with our increased interest in the operating company is taxed at our historical effective tax rate, exclusive of the adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders, the adjustments related to the non-recurring charges recognized in operating expenses, and other adjustments as noted above. Our effective tax rate, exclusive of these adjustments, was 36.7% for the year ended December 31, 2017 and approximately 36.8% and 37.1% for the years ended December 31, 2016 and 2015, respectively. See “Operating Results — Income Tax Expense/ (Benefit)” below.

TABLE OF CONTENTS

A reconciliation of the non-GAAP measures to the most comparable GAAP measures is included below:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands, except share and per share amounts)		
GAAP Net Income	$6,908	$16,179	$7,679
Net Expense as a result of Tax Cuts and Jobs Act	5,649	—	—
Impact of Change in Historical 754 Step-Up Calculations[1]	(1,006)	—	—
Net Effect of Tax Receivable Agreement	—	(8,221)	(424)
Net Effect of Non-Recurring Lease Expenses	—	—	183
Non-GAAP Net Income	$11,551	$7,958	$7,438
Basic Weighted Average Shares Outstanding	17,338,348	15,962,902	14,014,219
GAAP Basic Earnings per Share	$0.40	$1.01	$0.55
Net Expense as a result of Tax Cuts and Jobs Act	0.33	—	—
Impact of Change in Historical 754 Step-Up Calculations[1]	(0.06)	—	—
Net Effect of Tax Receivable Agreement	—	(0.51)	(0.03)
Net Effect of Non-Recurring Lease Expenses	—	—	0.01
Non-GAAP Basic Earnings per Share	$0.67	$0.50	$0.53
GAAP Net Income for Diluted Earnings per Share	$40,063	$39,600	$33,809
Net Expense as a result of Tax Cuts and Jobs Act	5,649	—	—
Impact of Change in Historical 754 Step-Up Calculations[1]	(1,006)	—	—
Net Effect of Tax Receivable Agreement	—	(8,221)	(1,148)
Net Effect of Non-Recurring Lease Expenses	—	—	1,834
Non-GAAP Net Income for Diluted Earnings per Share	$44,706	$31,379	$34,495
Basic Weighted Average Shares Outstanding	70,934,362	68,849,172	68,126,786
GAAP Diluted Earnings per Share	$0.56	$0.58	$0.50
Net Expense as a result of Tax Cuts and Jobs Act	0.08	—	—
Impact of Change in Historical 754 Step-Up Calculations[1]	(0.01)	—	—
Net Effect of Tax Receivable Agreement	—	(0.12)	(0.02)
Net Effect of Non-Recurring Lease Expenses	—	—	0.03
Non-GAAP Diluted Earnings per Share	$0.63	$0.46	$0.51

1 Reflects the net impact of a change in the calculation of historical 754 step-ups and related deferred tax asset and corresponding liability to selling and converting shareholders recognized during the year-ended December 31, 2017 as noted in the income tax expense/(benefit) discussion below.

Revenue

We generate revenue primarily from management fees and performance fees, which we collectively refer to as our advisory fees, by managing assets on behalf of our separately managed and sub-advised accounts, as well as our Pzena funds. Our advisory fee income is primarily based on our AUM, as discussed below, and is recognized over the period in which investment management services are provided. Following the preferred method identified in the Revenue Recognition Topic of the Financial Accounting Standards Board Accounting Standards Codification (“FASB ASC”), income from performance fees is recorded at the conclusion of the contractual performance period, when all contingencies are resolved.

Our advisory fees are primarily driven by the level of our AUM. Our AUM increases or decreases with the net inflows or outflows of funds into our various investment strategies and with the investment performance thereof. In order to increase our AUM and expand our business, we must develop and market investment strategies that suit the investment needs of our target clients, and provide attractive returns over the long-term. The value and composition of our AUM, and our ability to continue

28

to attract clients will depend on a variety of factors as described in “Item 1 — Risk Factors — Risks Related to Our Business — Our primary source of revenue is derived from management fees, which are directly tied to our assets under management. Fluctuations in AUM therefore will directly impact our revenue."

For our separately managed accounts, we are paid management fees according to a schedule, which varies by investment strategy. The substantial majority of these accounts pay us management fees pursuant to a schedule in which the rate we earn on the AUM declines as the amount of AUM increases.

Pursuant to our sub-investment advisory agreements with our clients and advisory agreements with Pzena-branded funds, we are generally paid a management fee according to a schedule in which the rate we earn on the AUM declines as the amount of AUM increases. Certain of these funds pay us fixed-rate management fees. Due to the substantially larger account size of certain of these sub-advised accounts, the average advisory fees we earn on them, as a percentage of AUM, are lower than the advisory fees we earn on our separately managed accounts.

Advisory fees we earn on separately managed accounts are generally based on the value of AUM at a specific date on a quarterly basis. Certain of our separately managed accounts, and all of our sub-advised accounts, are calculated based on the average of the monthly or daily market value. Advisory fees are also generally adjusted for any cash flows into or out of a portfolio, where the cash flow represents greater than 10% of the value of the portfolio. While a specific group of accounts may use the same fee rate, the calculation methodology may differ as described above.

Certain of our clients pay us performance fees according to the performance of their accounts relative to certain agreed-upon benchmarks, which results in a lower base fee, but allows for us to earn higher fees if the relevant investment strategy outperforms the agreed-upon benchmark. Some performance-based fee arrangements include high-water mark provisions, which generally provide that if a client account underperforms relative to its performance target, it must gain back such underperformance before we can collect future performance-based fees. Fulcrum fee arrangements related to one client relationship require a reduction in the base fee, or allow for a performance fee if the relevant investment strategy underperforms or outperforms, respectively, the agreed-upon benchmark.

Our advisory fees may fluctuate based on a number of factors, including the following:

- changes in AUM due to appreciation or depreciation of our investment portfolios, and the levels of the contribution and withdrawal of assets by new and existing clients;
- distribution of AUM among our investment strategies, which have differing fee schedules;
- distribution of AUM between separately managed accounts and sub-advised accounts, for which we generally earn lower overall advisory fees; and
- the level of our performance with respect to accounts on which we are paid performance fees or have fulcrum fee arrangements.

Expenses

Our expenses consist primarily of Compensation and Benefits Expense, as well as General and Administrative Expense. Our largest expense is Compensation and Benefits, which includes the salaries, bonuses, equity-based compensation, and related benefits and payroll costs attributable to our employee members and employees. Compensation and benefits packages are benchmarked against relevant industry and geographic peer groups in order to attract and retain qualified personnel. General and Administrative Expense includes lease expenses, professional and outside services fees, depreciation, costs associated with operating and maintaining our research, trading and portfolio accounting systems, and other expenses. Our occupancy-related costs and professional services expenses, in particular, generally increase or decrease in relative proportion to the overall size and scale of our business operations.

We incur additional expenses associated with being a public company for, among other things, director and officer insurance, director fees, SEC reporting and compliance (including Sarbanes-Oxley and Dodd-Frank compliance), professional fees, transfer agent fees, and other similar expenses.

Our expenses may fluctuate due to a number of factors, including the following:

TABLE OF CONTENTS

- variations in the level of total compensation expense due to, among other things, bonuses, awards of equity to our employees and employee members of our operating company, changes in our employee count and mix, and competitive factors; and

- general and administrative expenses, such as rent, professional service fees and data-related costs, incurred, as necessary, to run our business.

Other Income/ (Expense)

Other income/ (expense) is derived primarily from investment income or loss arising from our consolidated subsidiaries and interest income generated on our cash balances. Other income/ (expense) is also affected by changes in our estimates of the liability due to our selling and converting shareholders associated with payments owed to them under the tax receivable agreement which was executed in connection with our reorganization and initial public offering on October 30, 2007. As discussed further below under "Tax Receivable Agreement," this liability represents 85% of the amount of cash savings, if any, in U.S. federal, state, and local income tax that we realize as a result of the amortization of the increases in tax basis generated from our acquisitions of our operating company's units from our selling and converting shareholders. We expect the interest and investment components of other income/ (expense), in the aggregate, to fluctuate based on market conditions and the performance of our consolidated subsidiaries and other investments.

Non-Controlling Interests

We are the sole managing member of our operating company and control its business and affairs and, therefore, consolidate its financial results with ours. In light of our employees' and outside investors' direct and indirect interests in our operating company (as noted in "Item 1 — Business — Overview"), we have reflected their membership interests as a non-controlling interest in our consolidated financial statements. As of December 31, 2017, the holders of our Class A common stock and the holders of Class B units of our operating company held approximately 26.3% and 73.7%, respectively, of the economic interests in the operations of our business. In addition, our operating company consolidates the results of operations of the private investment partnerships and Pzena-branded mutual funds over which we exercise a controlling influence. Non-controlling interests recorded in our consolidated financial statements include the non-controlling interests of the outside investors in these consolidated subsidiaries.

Operating Results

Assets Under Management and Flows

As of December 31, 2017, our approximately $38.5 billion of AUM was invested in a variety of value-oriented investment strategies, representing distinct capitalization segments of U.S. and non-U.S. equity markets. The performance of our largest investment strategies as of December 31, 2017 is further described below. We follow the same investment process for each of these strategies. Our investment strategies are distinguished by the market capitalization ranges from which we select securities for their portfolios, which we refer to as each strategy's investment universe, as well as the regions in which we invest and the degree to which we concentrate on a limited number of holdings. While our investment process includes ongoing review of companies in the investment universes described below, our actual investments may include companies outside of the relevant market capitalization range at the time of our investment. In addition, the number of holdings typically found in the portfolios of each of our investment strategies may vary, as described below.

TABLE OF CONTENTS

The following tables describe the allocation of our AUM among our investment strategies and the domicile of our accounts, as of December 31, 2017, 2016 and 2015:

Strategy	AUM at December 31, 2017	2016	2015
	(in billions)		
U.S. Value Strategies			
Large Cap Value	$11.2	$9.4	$9.9
Mid Cap Value	2.8	2.5	1.8
Value	2.2	2.0	1.6
Small Cap Value	1.6	1.6	1.1
Other U.S. Strategies	0.1	0.1	0.1
Total U.S. Value Strategies	17.9	15.6	14.5
Global and Non-U.S. Value Strategies			
Global Value	6.7	4.6	4.2
International Value	6.3	4.9	4.2
Emerging Markets Value	4.3	2.6	1.8
European Value	3.2	2.1	1.1
Other Global and Non-U.S. Strategies	0.1	0.2	0.2
Total Global and Non-U.S. Value Strategies	20.6	14.4	11.5
Total	$38.5	$30.0	$26.0

Account Domicile	AUM at December 31, 2017	2016	2015
	(in billions)		
U.S.	$25.6	$21.1	$19.1
Non-U.S.	12.9	8.9	6.9
Total	$38.5	$30.0	$26.0

The following table indicates the annualized returns, gross and net (which represents annualized returns prior to, and after, payment of advisory fees, respectively), of our largest investment strategies from their inception to December 31, 2017, and in the five-year, three-year, and one-year periods ended December 31, 2017, relative to the performance of the market index which is often used by our clients to compare the performance of the relevant investment strategy.

Investment Strategy (Inception Date)	Period Ended December 31, 2017[1] Since Inception	5 Years	3 Years	1 Year
Large Cap Value (July 2012)				
Annualized Gross Returns	16.7%	16.6%	10.7%	17.9%
Annualized Net Returns	16.5%	16.4%	10.5%	17.7%
Russell 1000® Value Index	14.3%	14.0%	8.7 %	13.7%
International Value (November 2008)				
Annualized Gross Returns	12.1%	10.0%	9.4 %	25.5%
Annualized Net Returns	11.8%	9.7 %	9.1 %	25.1%
MSCI EAFE® Index – Net/U.S.$	8.7 %	7.9 %	7.8 %	25.0%
Large Cap Focused Value (October 2000)				

Annualized Gross Returns	8.0 %	16.7%	11.0%	18.2%
Annualized Net Returns	7.6 %	16.3%	10.6%	17.8%
Russell 1000® Value Index	7.1 %	14.0%	8.7 %	13.7%

31

TABLE OF CONTENTS

Emerging Markets Focused Value (January 2008)				
Annualized Gross Returns	4.0 %	6.3 %	11.0%	31.7%
Annualized Net Returns	3.2 %	5.5 %	10.2%	30.8%
MSCI® Emerging Markets Index – Net/U.S.$	1.7 %	4.4 %	9.1 %	37.3%
European Focused Value (August 2008)				
Annualized Gross Returns	7.0 %	10.2%	10.3%	30.1%
Annualized Net Returns	6.6 %	9.8 %	9.9 %	29.7%
MSCI® Europe Index – Net/U.S.$	3.2 %	7.4 %	6.7 %	25.5%
Global Value (January 2010)				
Annualized Gross Returns	10.3%	13.0%	10.0%	24.1%
Annualized Net Returns	10.0%	12.6%	9.6 %	23.7%
MSCI® World Index – Net/U.S.$	9.9 %	11.6%	9.3 %	22.4%
Global Focused Value (January 2004)				
Annualized Gross Returns	6.6 %	13.3%	10.0%	25.1%
Annualized Net Returns	5.9 %	12.6%	9.3 %	24.4%
MSCI® All Country World Index – Net/U.S.$	7.4 %	10.8%	9.3 %	24.0%
Mid Cap Value (April 2014)				
Annualized Gross Returns	11.3%	N/A	12.4%	14.2%
Annualized Net Returns	11.0%	N/A	12.1%	13.9%
Russell Mid Cap® Value Index	9.6 %	N/A	9.0 %	13.3%
Focused Value (January 1996)				
Annualized Gross Returns	11.4%	17.1%	11.3%	17.0%
Annualized Net Returns	10.6%	16.5%	10.6%	16.4%
Russell 1000® Value Index	9.1 %	14.0%	8.7 %	13.7%
Small Cap Focused Value (January 1996)				
Annualized Gross Returns	14.1%	16.8%	11.3%	4.8 %
Annualized Net Returns	12.9%	15.6%	10.2%	3.8 %
Russell 2000® Value Index	10.1%	13.0%	9.6 %	7.8 %
International Focused Value (January 2004)				
Annualized Gross Returns	7.5 %	10.7%	10.7%	27.8%
Annualized Net Returns	6.6 %	10.1%	10.1%	27.2%
MSCI® All Country World ex-U.S. Index – Net/U.S.$	6.8 %	6.8 %	7.8 %	27.2%
Mid Cap Focused Value (September 1998)				
Annualized Gross Returns	13.5%	17.7%	12.9%	15.8%
Annualized Net Returns	12.7%	17.0%	12.2%	15.1%
Russell Mid Cap® Value Index	10.8%	14.7%	9.0 %	13.3%

1 The historical returns of these investment strategies are not necessarily indicative of their future performance, or the future performance of any of our other current or future investment strategies.

2 Net of applicable withholding taxes and presented in U.S.$.

Large Cap Value. This strategy reflects a portfolio composed of approximately 50 to 80 stocks drawn generally from a universe of 500 of the largest U.S. listed companies, based on market capitalization. This strategy was launched in July 2012. At December 31, 2017, the Large Cap Value strategy generated a one-year annualized gross return of 17.9%, outperforming its benchmark. The outperformance was primarily driven by our stock selection in the producer durables and energy sectors.

International Value. This strategy reflects a portfolio composed of approximately 60 to 80 stocks drawn generally from a universe of 1,500 of the largest companies across the world excluding the United States, based on market capitalization. This strategy was launched in November 2008. At December 31, 2017, the International Value strategy generated a one-year

32

TABLE OF CONTENTS

annualized gross return of 25.5%, outperforming its benchmark. Although no individual factors had a significant influence on our performance, the largest positive contributors were our stock selection in the financial services sector as well as the performance of certain Korean stocks. These positive contributors were partially offset by our overexposure to the energy sector.

Large Cap Focused Value. This strategy reflects a portfolio composed of approximately 30 to 40 stocks drawn generally from a universe of 500 of the largest U.S. listed companies, based on market capitalization. This strategy was launched in October 2000. At December 31, 2017, the Large Cap Focused Value strategy generated a one-year annualized gross return of 18.2%, outperforming its benchmark. The outperformance was primarily driven by our stock selection in the producer durables and healthcare sectors.

Emerging Markets Focused Value. This strategy reflects a portfolio composed of approximately 40 to 80 stocks drawn generally from a universe of 1,500 of the largest emerging market companies, based on market capitalization. This strategy was launched in January 2008. At December 31, 2017, the Emerging Markets Focused Value strategy generated a one-year annualized gross return of 31.7%, underperforming its benchmark. The main contributors to this underperformance include our stock selection in the information technology sector as well as the performance of certain Chinese and Russian stocks. This underperformance was partially offset by our stock selection in the materials sector and the performance of certain Korean stocks.

European Focused Value. This strategy reflects a portfolio composed of approximately 40 to 50 stocks drawn generally from a universe of 750 of the largest European companies, based on market capitalization. This strategy was launched in August 2008. At December 31, 2017, the European Focused Value strategy generated a one-year annualized gross return of 30.1%, outperforming its benchmark. This outperformance was broad based and primarily driven by our stock selection in the materials sector and the performance of certain German and U.K. stocks, partially offset by our stock selection in the energy sector.

Global Value. This strategy reflects a portfolio composed of approximately 60 to 95 stocks drawn generally from a universe of 2,000 of the largest companies across the world, based on market capitalization. This strategy was launched in January 2010. At December 31, 2017, the Global Value strategy generated a one-year annualized gross return of 24.1%, outperforming its benchmark. This outperformance was primarily driven by our stock selection in the financial services sector as well as the performance of certain Korea stocks, partially offset by our stock selection in the information technology sector.

Global Focused Value. This strategy reflects a portfolio composed of approximately 40 to 60 stocks drawn generally from a universe of 2,000 of the largest companies across the world, based on market capitalization. This strategy was launched in January 2004. At December 31, 2017, the Global Focused Value strategy generated a one-year annualized gross return of 25.1%, outperforming its benchmark. This outperformance primarily driven by our stock selection in the materials sector, overexposure to the financial services sector, and the performance of certain Japanese stocks. This outperformance is partially offset by our stock selection in the information technology sector.

Mid Cap Value. This strategy reflects a portfolio composed of approximately 50 to 80 stocks drawn generally from a universe of U.S. listed companies ranked from the 201st to 1,200th largest, based on market capitalization. This strategy was launched in April 2014. At December 31, 2017, the Mid Cap Value strategy generated a one-year annualized gross return of 14.2%, outperforming its benchmark. This outperformance was primarily driven by our stock selection in the financial services and producer durables sectors.

Focused Value. This strategy reflects a portfolio composed of a portfolio of approximately 30 to 40 stocks drawn generally from a universe of 1,000 of the largest U.S. listed companies, based on market capitalization. This strategy was launched in January 1996. At December 31, 2017, the Focused Value strategy generated a one-year annualized gross return of 17.0%, outperforming its benchmark. The outperformance was driven primarily by our stock selection in the producer durables and healthcare sectors.

Small Cap Focused Value. This strategy reflects a portfolio composed of approximately 40 to 50 stocks drawn generally from a universe of U.S. listed companies ranked from the 1,001st to 3,000th largest, based on market capitalization. This strategy was launched in January 1996. At December 31, 2017, the Small Cap Focused Value strategy generated a one-year annualized gross return of 4.8%, underperforming its benchmark. This underperformance was primarily driven by our stock selection in the healthcare sector and our overexposure to the producer durables and technology sectors. This underperformance was partially offset by our stock selection in the materials sector.

TABLE OF CONTENTS

International Focused Value. This strategy reflects a portfolio composed of approximately 30 to 50 stocks drawn generally from a universe of 1,500 of the largest companies across the world excluding the United States, based on market capitalization. This strategy was launched in January 2004. At December 31, 2017, the International Focused Value strategy generated a one-year annualized gross return of 27.8%, outperforming its benchmark. The largest positive contributors were our stock selection in the financial services and materials sectors, partially offset by our stock selection in the information technology sector.

Mid Cap Focused Value. This strategy reflects a portfolio composed of approximately 30 to 40 stocks drawn generally from a universe of U.S. listed companies ranked from the 201st to 1,200th largest, based on market capitalization. This strategy was launched in September 1998. At December 31, 2017, the Mid Cap Focused Value strategy generated a one-year annualized gross return of 15.8%, outperforming its benchmark. The outperformance was driven primarily by our stock selection in the financial services sector and over exposure to the producer durables sector, partially offset by our stock selection in the energy sector.

Our earnings and cash flows are heavily dependent upon prevailing financial market conditions. Significant increases or decreases in the various securities markets, particularly the equities markets, can have a material impact on our results of operations, financial condition, and cash flows.

TABLE OF CONTENTS

In December 2017, we changed the classification of our AUM to better reflect the composition of our client base. We now group our assets into three new categories: separately managed accounts, sub-advised accounts, and Pzena funds, which better illustrate the characteristics inherent in our client relationships. Historical data has been reclassified for all periods presented and did not impact reported totals of AUM.

The change in AUM in our separately managed accounts, sub-advised accounts and Pzena funds for the years ended December 31, 2017, 2016, and 2015 is described below. Inflows are composed of the investment of new or additional assets by new or existing clients. Outflows consist of redemptions of assets by existing clients.

	For the Years Ended December 31,		
Assets Under Management[1]	2017	2016	2015
	(in billions)		
Separately Managed Accounts			
Assets			
Beginning of Period	$12.5	$11.0	$11.7
Inflows	1.4	1.7	2.3
Outflows	(1.6)	(2.0)	(2.4)
Net Flows	(0.2)	(0.3)	(0.1)
Market Appreciation/(Depreciation)	2.7	1.8	(0.6)
End of Period	$15.0	$12.5	$11.0
Sub-Advised Accounts			
Assets			
Beginning of Period	$16.3	$14.1	$15.0
Inflows	3.5	2.6	1.9
Outflows	(1.8)	(2.9)	(2.1)
Net Flows	1.7	(0.3)	(0.2)
Market Appreciation/(Depreciation)	3.8	2.5	(0.7)
End of Period	$21.8	$16.3	$14.1
Pzena Funds			
Assets			
Beginning of Period Assets	$1.2	$0.9	$1.0
Inflows	0.5	0.3	0.2
Outflows	(0.3)	(0.2)	(0.2)
Net Flows	0.2	0.1	—
Market Appreciation/(Depreciation)	0.3	0.2	(0.1)
End of Period	$1.7	$1.2	$0.9
Total			
Assets			
Beginning of Period	$30.0	$26.0	$27.7
Inflows	5.4	4.6	4.4
Outflows	(3.7)	(5.1)	(4.7)
Net Flows	1.7	(0.5)	(0.3)
Market Appreciation/(Depreciation)	6.8	4.5	(1.4)
End of Period	$38.5	$30.0	$26.0

During the year ended December 31, 2017, our AUM increased $8.5 billion, or 28.3%, from $30.0 billion at December 31, 2016. This increase is primarily due to market appreciation and net inflows during the year ended December 31, 2017.

At December 31, 2017, we managed $15.0 billion in separately managed accounts, $21.8 billion in sub-advised accounts, and $1.7 billion in Pzena funds, for a total of $38.5 billion in assets. For the year ended December 31, 2017, we experienced $6.8 billion in market appreciation and total gross inflows of $5.4 billion, which were partially offset by total gross outflows of

35

TABLE OF CONTENTS

$3.7 billion. Assets in separately managed accounts increased by $2.5 billion, or 20.0%, from $12.5 billion at December 31, 2016, due to $2.7 billion in market appreciation and $1.4 billion in gross inflows, partially offset by $1.6 billion in gross outflows. Assets in sub-advised accounts increased by $5.5 billion, or 33.7%, from $16.3 billion at December 31, 2016, due to $3.8 billion in market appreciation and $3.5 billion in gross inflows, partially offset by $1.8 billion in gross outflows. Assets in Pzena funds increased by $0.5 billion, or 41.7%, from $1.2 billion at December 31, 2016 as a result of $0.5 billion in gross inflows and $0.3 billion in market appreciation, partially offset by $0.3 billion in gross outflows.

At December 31, 2016, we managed $12.5 billion in separately managed accounts, $16.3 billion in sub-advised accounts, and $1.2 billion in Pzena funds, for a total of $30.0 billion in assets. For the year ended December 31, 2016, we experienced total gross inflows of $4.6 billion and $4.5 billion in market appreciation, which were partially offset by total gross outflows of $5.1 billion. Assets in separately managed accounts increased by $1.5 billion, or 13.6%, from $11.0 billion at December 31, 2015, due to $1.8 billion in market appreciation and $1.7 billion in gross inflows, partially offset by $2.0 billion in gross outflows. Assets in sub-advised accounts increased $2.2 billion, or 15.6%, from $14.1 billion at December 31, 2015, due to $2.6 billion in gross inflows and $2.5 billion in market appreciation, partially offset by $2.9 billion in gross outflows. Assets in Pzena funds increased by $0.3 billion, or 33.3%, from $0.9 billion at December 31, 2015 as a result of $0.3 billion in gross inflows and $0.2 billion in market appreciation, partially offset by $0.2 billion in gross outflows.

At December 31, 2015, we managed $11.0 billion in separately managed accounts, $14.1 billion in sub-advised accounts, and $0.9 billion in Pzena funds, for a total of $26.0 billion in assets. For the year ended December 31, 2015, we experienced total gross outflows of $4.7 billion and market depreciation of $1.4 billion, which were partially offset by total gross inflows of $4.4 billion. Assets in separately managed accounts decreased by $0.7 billion, or 6.0%, from $11.7 billion at December 31, 2014 due to $2.4 billion in gross outflows and $0.6 billion in market depreciation, partially offset by $2.3 billion in gross inflows. Assets in sub-advised accounts decreased $0.9 billion, or 6.0%, from $15.0 billion at December 31, 2014, due to $2.1 billion in gross outflows and $0.7 billion in market depreciation, partially offset by $1.9 billion in gross inflows. Assets in Pzena funds decreased by $0.1 billion, or 10.0%, from $1.0 billion at December 31, 2014, as a result of $0.2 billion in gross outflows and $0.1 billion in market depreciation, partially offset by $0.2 billion in gross inflows.

Revenue

Our revenue from advisory fees earned on our separately managed accounts, sub-advised accounts and Pzena funds for the three years ended December 31, 2017 is described below:

	For the Years Ended December 31,		
Revenue	2017	2016	2015
	(in thousands)		
Separately Managed Accounts	$76,419	$61,165	$68,213
Sub-Advised Accounts	55,003	40,018	41,980
Pzena Funds	9,873	7,153	6,414
Total	$141,295	$108,336	$116,607

Year Ended December 31, 2017 versus December 31, 2016

Our total revenue increased $33.0 million, or 30.4%, to $141.3 million for the year ended December 31, 2017 from $108.3 million for the year ended December 31, 2016. This change was driven by an increase in average assets during 2017, as well as an increase in performance fees recognized during 2017. We recognized $3.2 million in performance fees during 2017 as compared to $0.2 million in performance fees recognized in 2016. In addition, we recognized a

$1.0 million reduction in base fees related to fulcrum fee arrangements for the year ended December 31, 2016. For the year ended December 31, 2017, we did not recognize a reduction in base fees related to fulcrum fee arrangements. Average AUM increased 26.6% to $33.8 billion as of December 31, 2017 from $26.7 billion as of December 31, 2016.

Our weighted average fee rates were 0.418% and 0.406% for the years ended December 31, 2017 and 2016, respectively. Average assets in separately managed accounts increased 24.5% to $13.7 billion for the year ended December 31, 2017, from $11.0 billion for the year ended December 31, 2016, and had weighted average fees of 0.556% and 0.555% for the years ended December 31, 2017 and 2016, respectively. Average assets in sub-advised accounts increased 27.4% to $18.6 billion for the year ended December 31, 2017, from $14.6 billion for the year ended December 31, 2016, and had weighted average fees of 0.295% and 0.273% for the years ended December 31, 2017 and 2016, respectively. The increase in weighted average fees in sub-advised accounts was due primarily to a increase in performance fees recognized in 2017 and the reduction of base fees related to the fulcrum fee arrangements of certain accounts related to one client relationship recognized in 2016. A reduction in base fees was not recognized during 2017. Average assets in Pzena funds increased 50.0% to $1.5 billion for the year ended December 31, 2017, from $1.0 billion for the year ended December 31, 2016, and had weighted average fees of 0.679% and 0.687% for the years ended December 31, 2017 and 2016, respectively.

Year Ended December 31, 2016 versus December 31, 2015

Our total revenue decreased $8.3 million, or 7.1%, to $108.3 million for the year ended December 31, 2016, from $116.6 million for the year ended December 31, 2015. This change was driven by a decrease in performance fees recognized during 2016, a decrease in average assets, as well as a reduction in base fees associated with fulcrum fee arrangements. We recognized $0.2 million in performance fees during 2016 as compared to $4.5 million in performance fees recognized in 2015. We recognized a $1.0 million reduction in base fees related to fulcrum fee arrangements for the year ended December 31, 2016. For the year ended December 31, 2015, we did not recognize a reduction in base fees related to fulcrum fee arrangements. Average AUM decreased 2.6% to $26.7 billion as of December 31, 2016 from $27.4 billion as of December 31, 2015.

Our weighted average fee rates were 0.406% and 0.426% for the years ended December 31, 2016 and 2015, respectively. Average assets in separately managed accounts decreased 6.0%, to $11.0 billion for the year ended December 31, 2016, from $11.7 billion for the year ended December 31, 2015, and had weighted average fees of 0.555% and 0.582% for the years ended December 31, 2016 and 2015, respectively. The decrease in weighted average fees in separately managed accounts was due primarily to a decrease in performance fees recognized in 2016. Average assets in sub-advised accounts was $14.7 billion for the year ended December 31, 2016, in-line with $14.7 billion for the year ended December 31, 2015, and had weighted average fees of 0.273% and 0.285% for the years ended December 31, 2016 and 2015, respectively. The decrease in weighted average fees in sub-advised accounts was due primarily to a decrease in performance fees recognized in 2016 and the reduction of base fees related to the fulcrum fee arrangements of certain accounts related to one client relationship. Average assets in Pzena funds was $1.0 billion for the year ended December 31, 2016, in-line with $1.0 billion for the year ended December 31, 2015, and had weighted average fees of 0.687% and 0.674% for the years ended December 31, 2016 and 2015, respectively. The increase in weighted average fees in Pzena funds was due to the opening of non-U.S. funds during 2016 that generally carry higher fee rates.

Expenses

Our operating expense is driven primarily by our compensation costs. The table below describes the components of our operating expense for the years ended December 31, 2017, 2016, and 2015.

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Cash Compensation and Other Benefits	$48,722	$41,397	$35,431
Other Non-Cash Compensation	10,182	6,933	11,092
Total Compensation and Benefits Expense	58,904	48,330	46,523
General and Administrative Expense	13,337	12,788	14,667
Total Operating Expenses	$72,241	$61,118	$61,190

Year Ended December 31, 2017 versus December 31, 2016

Total operating expenses increased by $11.1 million, or 18.2%, to $72.2 million for the year ended December 31, 2017, from $61.1 million for the year ended December 31, 2016.

Compensation and benefits expense increased by $10.6 million, or 21.9%, to $58.9 million for the year ended December 31, 2017, from $48.3 million for the year ended December 31, 2016. This increase reflects an increase in compensation rates, certain awards issued in the beginning of 2017, and an increase in obligations under our deferred compensation plan driven by an increase in the performance of the strategies in which employees elected to invest deferred compensation. We would expect non-cash compensation expense in subsequent years to depend on the size and composition of awards granted under our equity incentive plans as well as levels of deferred compensation.

General and administrative expense increased by $0.5 million, or 4.3%, to $13.3 million for the year ended December 31, 2017, from $12.8 million for the year ended December 31, 2016. This increase primarily reflects an increase in professional fees and travel expenses.

Year Ended December 31, 2016 versus December 31, 2015

Total operating expense decreased by $0.1 million, or 0.1%, to $61.1 million for the year ended December 31, 2016, from $61.2 million for the year ended December 31, 2015.

Compensation and benefits expense increased by $1.8 million, or 3.9%, to $48.3 million for the year ended December 31, 2016, from $46.5 million for the year ended December 31, 2015. This increase reflects an increase in compensation and headcount, as well as an increase in obligations under our deferred compensation plan driven by an increase in the performance of the strategies in which employees elected to invest deferred compensation. We would expect non-cash compensation expense in subsequent years to depend on the size and composition of awards granted under our equity incentive plans. The fluctuation between cash and non-cash compensation expense from December 31, 2015 to December 31, 2016 reflects $4.5 million of cash compensation paid in the form Delayed Exchange Class B units and Class B units which were issued and vested immediately on January 1, 2017. For the year ended December 31, 2015 such elections were issued and vested immediately in December 2015 and were reflected in non-cash compensation expenses.

General and administrative expense decreased by $1.9 million, or 12.8%, to $12.8 million for the year ended December 31, 2016, from $14.7 million for the year ended December 31, 2015. This decrease primarily reflects $1.8 million in non-recurring losses and lease expenses associated with the exit from our former corporate headquarters in the first half of 2015 and certain other operational expenses that did not recur during 2016, partially offset by an increase in expenses during 2016 associated with new business initiatives.

Other Income/ (Expense)

Year Ended December 31, 2017 versus December 31, 2016

Other income/ (expense) was $25.6 million for the year ended December 31, 2017, and consisted primarily of $20.8 million in income related to adjustments to our liability to our selling and converting shareholders, $2.6 million in net realized and unrealized gains from investments, $1.5 million in equity in the earnings of affiliates, and $0.6 million in interest and dividend income. Other income/ (expense) was an expense of $48.0 million for the year ended December 31, 2016, and consisted primarily of $51.4 million in expense related to adjustments to our liability to our selling and converting shareholders, partially offset by $1.8 million in net realized and unrealized gains from investments, $1.2 million in equity in the earnings of affiliates, and $0.4 million in interest and dividend income. As discussed further below, the liability to our selling and converting shareholders represents 85% of the amount of cash savings, if any, in U.S. federal, state and local income tax that we realize as a result of the amortization of the increases in tax basis generated from our purchase of operating company units from our selling shareholders. The decrease in the liability to our selling and converting shareholders primarily resulted from the re-measurement of the deferred tax asset upon enactment of the Tax Cuts and Jobs Act in the fourth quarter of 2017 described in income tax expense/ (benefit) below.

Year Ended December 31, 2016 versus December 31, 2015

Other income/ (expense) was an expense of $48.0 million for the year ended December 31, 2016, and consisted primarily of $51.4 million in expense related to adjustments to our liability to our selling and converting shareholders, partially offset by $1.8 million in net realized and unrealized gains from investments, $1.2 million in equity in the earnings of affiliates, and $0.4 million in interest and dividend income. Other income/ (expense) was an expense of $3.3 million for the year ended December 31, 2015, and consisted primarily of $3.2 million in net realized and unrealized losses from investments and $0.4 million in expense related to adjustments to our liability to our selling and converting shareholders, partially offset by $0.8 million in interest and dividend income. As discussed further below, the liability to our selling and converting shareholders represents 85% of the amount of cash savings, if any, in U.S. federal, state and local income tax that we realize as a result of the amortization of the increases in tax basis generated from our purchase of operating company units from our selling shareholders. The increase in the liability to our selling and converting shareholders resulted from the release of the valuation allowance recorded against the deferred tax assets described in income tax expense/ (benefit) below. The $6.4 million year-over-year change in gains and other investment income was due to performance of our direct investments, the majority of which are held to satisfy obligations under its deferred compensation plan, as well as gains recognized by external investors on their investments in our consolidated subsidiaries.

TABLE OF CONTENTS

Income Tax Expense/ (Benefit)

For the years ended December 31, 2017, 2016, and 2015, components of income tax expense/ (benefit) are as follows:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Unincorporated and Other Business Tax Expenses	$2,862	$1,588	$2,228
Corporate Tax Expense/ (Benefit):			
Corporate Income Tax Expense	6,188	3,935	4,160
Impact of Tax Cuts and Jobs Act[1]	26,468	—	—
Change in the Valuation Allowance	—	(61,942)	(1,274)
Impact of Change in Historical 754 Step-Up Calculations[2]	(1,006)	—	—
Net Adjustment to Deferred Tax Asset	—	1,944	—
Total Corporate Tax Expense/ (Benefit)	31,650	(56,063)	2,886
Total Income Tax Expense/ (Benefit)	$34,512	$(54,475)	$5,114

1 Reflects income tax expense resulting from the re-measurement of the deferred tax asset related to the Tax Cuts and Jobs Act enacted in the United States during the fourth quarter of 2017.

2 Reflects the net impact of a change in the calculation of historical 754 step-ups and related deferred tax asset and corresponding liability to selling and converting shareholders recognized during the year-ended December 31, 2017.

Our results for the years ended December 31, 2017, 2016, and 2015 included the effects of adjustments related to the Tax Cuts and Jobs Act, our tax receivable agreement and the associated liability, as well as non-recurring lease expenses discussed in “Expenses,” above. Details of corporate tax expenses excluding these items and reconciliations between our GAAP and non-GAAP corporate tax items are as follows:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Corporate Tax Expense/ (Benefit)	$31,650	$(56,063)	$2,886
Less: Impact of Tax Cuts and Jobs Act	(26,468)	—	—
Less: Effects of One Time Adjustments	—	—	132
Less: Change in the Valuation Allowance Associated with the Tax Receivable Agreement	—	61,607	847
Less: Impact of Change in Historical 754 Step-Up Calculations	1,006	—	—
Less: Net Adjustment to Deferred Tax Assets Associated with the Tax Receivable Agreement	—	(1,944)	—
Non-GAAP Corporate Income Tax Expense	$6,188	$3,600	$3,865

Our effective tax rate, exclusive of adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders and adjustments related to non-recurring expenses recognized in operating expense in the fourth quarter of 2015, was 34.9%, 31.1%, and 34.2% for the years ended December 31, 2017, 2016, and 2015, respectively, and was determined as follows:

	For the Years Ended December 31,					
	2017		2016		2015	
	Tax	% of Non-GAAP Pre-tax	Tax	% of Non-GAAP Pre-tax	Tax	% of Non-GAAP Pre-tax

	Income (in thousands)		Income (in thousands)		Income (in thousands)	
Federal Corporate Tax	$6,031	34.0 %	$3,930	34.0 %	$3,843	34.0 %
State and Local Taxes, Net of Federal Benefit	479	2.7 %	325	2.8 %	350	3.1 %
Prior Period and Other Adjustments	(322)	(1.8)%	(655)	(5.7)%	(328)	(2.9)%
Non-GAAP Effective Taxes	$6,188	34.9 %	$3,600	31.1 %	$3,865	34.2 %

A comparison of the GAAP effective tax rates for the years ended December 31, 2017, 2016, and 2015 is not meaningful due to the Tax Cuts and Jobs Act and valuation allowance adjustments.

Year Ended December 31, 2017 versus December 31, 2016

Income tax expense/ (benefit) was an expense of $34.5 million for the year ended December 31, 2017, compared to $54.5 million in income tax benefit for the year ended December 31, 2016. The 2017 income tax expense included $26.5 million of expense related to the re-measurement of the deferred tax asset upon enactment of the Tax Cuts and Jobs Act in the United States during the fourth quarter of 2017. Additionally, we identified an adjustment related to the historical calculation of the 754 step-ups in tax basis impacting the deferred tax assets and corresponding liability to selling and converting shareholders. The adjustment was made during the year-ended December 31, 2017, resulting in a $4.6 million decrease to the deferred tax assets and a $5.6 million decrease to the corresponding liability to selling and converting shareholders. The cumulative impact of the adjustment is a net tax benefit of approximately $1.0 million which was recognized as a component of income tax expense/(benefit) for the year ended December 31, 2017.

The 2016 income tax benefit included $61.9 million of benefit associated with the release of the valuation allowance recorded against our deferred tax asset during the fourth quarter of 2016. The 2016 income tax benefit also reflects a $1.9 million adjustment associated with the net impact of the changes in the deferred tax asset and valuation allowance assessed against the deferred tax asset associated with the changes in expected future tax benefits. Exclusive of these adjustments, the remaining income tax expense for the year ended December 31, 2017 consisted of $2.9 million in operating company unincorporated and other business tax expenses and $6.2 million of corporate income tax expenses. On a similar basis, the remaining income tax expense for the year ended December 31, 2016 consisted of $1.6 million of operating company unincorporated business tax expenses and $3.9 million of corporate income tax expenses. The increase in operating company unincorporated and other business tax expenses reflects a $0.7 million benefit associated with the reversal of uncertain tax position liabilities and interest due to the settlement of prior year audits during 2016.

Year Ended December 31, 2016 versus December 31, 2015

Income tax expense/ (benefit) was a benefit of $54.5 million for the year ended December 31, 2016, compared to $5.1 million in income tax expense for the year ended December 31, 2015. The 2016 and 2015 income tax expense/ (benefit) included $61.9 million and $1.3 million, respectively, of benefit associated with adjustments to the valuation allowance recorded against our deferred tax asset. The increase in the benefit associated with the change in the valuation allowance reflects the release of the valuation allowance during 2016 resulting from increased levels of assets under management and the associated future taxable income used to analyze the realizability of the deferred tax asset. As of December 31, 2016, the Company concluded it is more-likely-than-not that it will generate sufficient taxable income in the future to realize its deferred tax asset. The 2016 income tax benefit also reflects a $1.9 million adjustment associated with the net impact of the changes in the deferred tax asset and valuation allowance assessed against the deferred tax asset associated with the changes in expected future tax benefits. Exclusive of these adjustments, the remaining income tax expense/ (benefit) for the year ended December 31, 2016 consisted of $1.6 million in operating company unincorporated and other business tax expenses and $3.9 million of corporate income tax expenses. On a similar basis, the remaining income tax expense/ (benefit) for the year ended December 31, 2015 consisted of $2.2 million of operating company unincorporated business tax expenses and $4.2 million of corporate income tax expenses. The decrease in operating company unincorporated and other business tax expenses reflects a $0.7 million benefit associated with the reversal of uncertain tax position liabilities and interest due to the settlement of prior year audits.

40

TABLE OF CONTENTS

Net Income Attributable to Non-Controlling Interests

Year Ended December 31, 2017 versus December 31, 2016

Net income attributable to non-controlling interests was $53.2 million for the year ended December 31, 2017, and consisted of $52.4 million associated with our employees' and outside investors' approximately 74.7% weighted-average interest in the income of the operating company, and approximately $0.9 million associated with our consolidated subsidiaries' interest in the income of our consolidated subsidiaries. Net income attributable to non-controlling interests was $37.5 million for the year ended December 31, 2016, and consisted of $37.1 million associated with our employees’ and outside investors’ approximately 76.3% weighted-average interest in the income of the operating company, and approximately $0.4 million associated with our consolidated subsidiaries’ interest in the income of our consolidated subsidiaries. The change in net income attributable to non-controlling interests primarily reflects the increase in net income of the operating company for the year ended December 31, 2017, partially offset by a decrease in our employees’ and outside investors’ weighted average interest in the income of the operating company. We expect the interests in our operating company in subsequent periods to depend on changes in our shareholder’s equity and the size and composition of Class B units awarded by our operating company’s compensation plans.

Year Ended December 31, 2016 versus December 31, 2015

Net income attributable to non-controlling interests was $37.5 million for the year ended December 31, 2016, and consisted of $37.1 million associated with our employees' and outside investors' approximately 76.3% weighted-average interest in the income of the operating company, and approximately $0.4 million associated with our consolidated subsidiaries' interest in the income of our consolidated subsidiaries. Net income attributable to non-controlling interests was $39.3 million for the year ended December 31, 2015, and consisted of $41.6 million associated with our employees’ and outside investors’ approximately 78.8% weighted-average interest in the income of the operating company, partially offset by $2.2 million associated with our consolidated subsidiaries’ interest in the losses of our consolidated subsidiaries. The change in net income attributable to non-controlling interests primarily reflects the decrease in net income of the operating company for the year ended December 31, 2016, and the decrease in our employees’ and outside investors’ weighted average interest in the income of the operating company. We expect the interests in our operating company in subsequent periods to depend on changes in our shareholder’s equity and the size and composition of Class B units awarded by our operating company’s compensation plans.

Liquidity and Capital Resources

Historically, the working capital needs of our business have primarily been met through the cash generated by our operations. Distributions to members of our operating company are our largest use of cash. Other activities include purchases and sales of investments to fund our deferred compensation program, capital expenditures, and strategic growth initiatives such as providing the seed investments in our mutual funds.

We expect to fund the liquidity needs of our business in the next twelve months, and over the long-term, primarily through cash generated from operations. As an investment management company, our business is materially affected by conditions in the global financial markets and economic conditions throughout the world. Our liquidity is highly dependent on the revenue and income from our operations, which is directly related to our levels of AUM. For the year ended December 31, 2017, our average AUM and revenues increased by 26.6% and 30.4%, respectively, compared to our average AUM and revenues for the year ended December 31, 2016. At December 31, 2017, our cash was $63.4 million, inclusive of $6.4 million in cash held by our consolidated subsidiaries. Advisory fees receivable was $32.5 million. We also had approximately $11.2 million in investments set aside to satisfy our obligations under our deferred compensation program.

In determining the sufficiency of liquidity and capital resources to fund our business, we regularly monitor our liquidity position, including, among other things, cash, working capital, investments, long-term liabilities, lease commitments, debt obligations, and operating company distributions. Compensation is our largest expense. To the extent we deem necessary and appropriate to run our business, recognizing the need to retain our key personnel, we have the ability to change the absolute levels of our compensation packages, as well as change the mix of their cash and non-cash components. Historically, we have not tied our level of compensation directly to revenue, as many Wall Street firms do. Correspondingly, there is not a linear relationship between our compensation and the revenues we generate. This generally has the effect of increasing operating margins in periods of increased revenues, but can reduce operating margins when revenue declines.

We continuously evaluate our staffing requirements and compensation levels with reference to our own liquidity position and external peer benchmarking data. The result of this review directly influences management’s recommendations to our Board of Directors with respect to such staffing and compensation levels.

We anticipate that tax allocations and dividend equivalent payments to the members of our operating company, which consists of certain of our employees, unaffiliated persons, former employees, and us, will continue to be a material financing activity. Cash distributions to operating company members for partnership tax allocations would increase should the taxable income of the operating company increase. Dividend equivalent payments will depend on our dividend policy and the discretion of our Board of Directors, as discussed below.

We believe that our lack of long-term debt, and ability to vary cash compensation levels, have provided us with an appropriate degree of flexibility in providing for our liquidity needs.

Dividend Policy

As we are a holding company and have no material assets other than our ownership of membership interests in our operating company, we depend upon distributions from our operating company to pay any dividends that our Board of Directors may declare to be paid to our Class A common stockholders. When, and if, our Board of Directors declares any such dividends, we then cause our operating company to make distributions to us in an amount sufficient to cover the dividends declared. Our dividend policy has certain risks and limitations, particularly with respect to liquidity. We may not pay dividends to our Class A common shareholders in amounts that have been paid to them in the past, or at all, if, among other things, we do not have the cash necessary to pay our intended dividends. To the extent we do not have cash on hand sufficient to pay dividends in the future, we may decide not to pay dividends. By paying cash dividends rather than investing that cash in our future growth, we risk slowing the pace of our growth, or not having a sufficient amount of cash to fund our operations or unanticipated capital expenditures, should the need arise.

On January 30, 2018, the Company's Board of Directors determined that it intends to reduce the targeted cash dividend payout ratio from 70% to 80% of non-GAAP diluted net income to 60% to 70% of non-GAAP diluted net income. Barring any changes in the Company’s financial condition, with the beneficial impact of the lower future effective tax rate due to the corporate tax rates enacted in the Tax Cuts and Jobs Act of 2017, we should expect to maintain the absolute level of the dividend despite the reduction in payout ratio. The Board regularly reviews the Company's long-term capital allocation strategy and determined that it is prudent to have additional financial flexibility to allow for investment in future business initiatives, while still returning a meaningful cash dividend to shareholders.

Our ability to pay dividends is subject to the Board of Directors’ discretion and may be limited by our holding company structure and applicable provisions of Delaware law. See “Item 1A — Risk Factors — Risks Relating to Our Class A Common Stock — Our ability to pay dividends is subject to the discretion of our Board of Directors and may be limited by our holding company structure and applicable provisions of Delaware law.”

Tax Receivable Agreement

Our purchase of membership units of our operating company concurrent with our IPO, and the subsequent and future exchanges by holders of Class B units of our operating company for shares of our Class A common stock (pursuant to the exchange rights provided for in the operating company’s operating agreement), has resulted in, and is expected to continue to result in, increases in our share of the tax basis of the tangible and intangible assets of our operating company, which will increase the tax depreciation and amortization deductions that otherwise would not have been available to us. These increases in tax basis and tax depreciation and amortization deductions have reduced, and are expected to continue to reduce, the amount of cash taxes that we would otherwise be required to pay in the future. We have entered into a tax receivable agreement with the current members of our operating company, the one member of our operating company immediately prior to our initial public offering who sold all of its membership units to us in connection with our initial public offering, and any future holders of Class B units, that requires us to pay them 85%

of the amount of cash savings, if any, in U.S. federal, state and local income tax that we actually realize (or are deemed to realize in the case of an early termination payment by us, or a change in control, as described in the tax receivable agreement) as a result of the increases in tax basis described above and certain other tax benefits related to entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement.

TABLE OF CONTENTS

Cash Flows

Year Ended December 31, 2017 versus December 31, 2016

Cash increased $19.9 million to $63.4 million in 2017 compared to $43.5 million in 2016. Net cash provided by operating activities increased $12.7 million in 2017 to $67.7 million from $58.6 million in 2016. The increase primarily reflects an increase in net income, changes in the levels of non-cash compensation, equity in the earnings of affiliates, net realized and unrealized gains from investments, as well as changes in operating assets and liabilities and working capital.

Net cash provided by investing activities was $0.5 million in 2017 compared to $0.2 million in 2016. The $0.3 million increase was primarily due to a $1.1 million increase in proceeds from net sales of investments, partially offset by a $0.5 million increase in payments to related parties related primarily to loans made to employees.

Net cash used in financing activities decreased $2.4 million in 2017 to $48.0 million from $50.4 million in 2016. This decrease is primarily due to a $1.6 million decrease in the repurchase and retirement of shares of Class A common stock and Class B units during 2017 and a $2.0 million decrease in net distributions from non-controlling interests, partially offset by a $0.9 million decrease in cash provided by option exercises.

Year Ended December 31, 2016 versus December 31, 2015

Cash increased $8.1 million to $43.5 million in 2016 compared to $35.4 million in 2015. Net cash provided by operating activities increased $1.2 million in 2016 to $58.6 million from $57.4 million in 2015. The increase primarily reflects a change in the timing of year-end bonus payments to January of the subsequent year as well as an increase in net income driven by taxes, changes in the liability to selling and converting shareholders, and gains/ losses and other investment income. These increases were partially offset by changes in operating assets and liabilities and working capital.

Net cash provided by investing activities was $0.2 million in 2016 compared to $6.2 million used in 2015. The $6.4 million increase was primarily due to a $6.2 million decrease in cash used in the purchases of property and equipment and a $1.0 million decrease in payments to related parties related primarily to loans made to employees in December of 2015, partially offset by $0.8 million decrease in proceeds from net sales of investments.

Net cash used in financing activities decreased $4.5 million in 2016 to $50.4 million from $54.9 million in 2015. This decrease is primarily due to a $4.4 million decrease in the repurchase and retirement of shares of Class A common stock and Class B units during 2016.

Contractual Obligations

The following table sets forth information regarding our consolidated contractual obligations as of December 31, 2017.

	Payments Due by Period				
	Total	Less Than 1 Year	1 – 3 Years	3 – 5 Years	More Than 5 Years
	(in thousands)				
Operating Lease Expenses, Net of Sublease Rental Income	$15,353	$1,618	$3,838	$5,938	$3,959
Total	$15,353	$1,618	$3,838	$5,938	$3,959

Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of December 31, 2017.

TABLE OF CONTENTS

Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"), requires management to make estimates and judgments that affect our reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under current circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily available from other sources. We evaluate our estimates on an ongoing basis. Actual results may differ from these estimates under different assumptions or conditions.

Accounting policies are an integral part of our financial statements. A thorough understanding of these accounting policies is essential when reviewing our reported results of operations and our financial condition. Management believes that the critical accounting policies discussed below involve additional management judgment due to the sensitivity of the methods and assumptions used.

Consolidation

Our policy is to consolidate all majority-owned subsidiaries in which we have a controlling financial interest and variable-interest entities of which we are deemed to be the primary beneficiary. We assess our consolidation practices regularly, as circumstances dictate. All significant inter-company transactions and balances have been eliminated.

Income Taxes

We are a “C” corporation under the Internal Revenue Code, and thus liable for federal, state and local taxes on the income derived from our economic interest in our operating company. The operating company is a limited liability company that has elected to be treated as a partnership for tax purposes. Our operating company has not made a provision for federal or state income taxes because it is the responsibility of each of the operating company’s members (including us) to separately report their proportionate share of the operating company’s taxable income or loss. Similarly, the income of our consolidated investment partnerships is not subject to income taxes, as such income is allocated to each partnership’s individual partners. The operating company has made a provision for New York City Unincorporated Business Tax (UBT) and its consolidated subsidiary Pzena Investment Management, LTD has made a provision for U.K. income taxes.

We recognize deferred tax assets and liabilities for the future tax consequences attributable to differences between the carrying amounts of existing assets and liabilities and their respective tax bases, net operating loss carryforwards and tax credits. A valuation allowance is recorded on our deferred tax assets when it is more-likely-than-not that all or a portion of such assets will not be realized. When evaluating the realizability of our deferred tax assets, all evidence, both positive and negative, is evaluated, which requires management to make significant judgments and assumptions. Items considered when evaluating the need for a valuation allowance include our forecast of future taxable income, future reversals of existing temporary differences, tax planning strategies and other relevant considerations.

We believe that the accounting estimate related to the valuation allowance is a critical accounting estimate because the underlying assumptions can change from period to period. For example, tax law changes, or variances in future projected operating performance, could result in a change in the valuation allowance. Each quarter, we re-evaluate our estimate related to the valuation allowance, including our assumptions about future taxable income. If we are not able to realize all or part of our net deferred tax assets in the future, a valuation allowance would be recorded against our deferred tax asset and charged to income tax expense in the period such determination was made.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting." The Company adopted ASU No. 2016-09 as of January 1, 2017. This standard requires excess tax benefits and tax deficiencies to be recorded in the consolidated statements of operations as a component of Income Tax Expense when equity awards vest or are settled. The Company is no longer required to delay recognition of an excess tax benefit until it reduces current taxes payable. The standard also requires excess tax benefits to be classified as operating activities along with other income tax cash flows within the consolidated statements of cash flows. In addition, ASU No. 2016-09 allows entities to make an accounting policy election to either estimate the number of forfeitures expected to occur, as was previously required, or to account for actual forfeitures as they occur. The Company has elected to account for forfeitures as they occur, rather than estimate expected forfeitures.

TABLE OF CONTENTS

The adoption of ASU No. 2016-09 resulted in a net cumulative effect adjustment reflecting a $1.4 million increase to retained earnings and the deferred tax asset as of January 1, 2017, related to the recognition of the previously unrecognized excess tax benefits using the modified retrospective method. Estimates of forfeitures in prior periods were immaterial, and therefore are not included in the cumulative effect adjustment. The amendments related to the classification of the excess tax benefits in the consolidated statements of cash flows were adopted on a prospective basis, which did not require the restatement of prior periods.

Management judgment is required in determining our provision for income taxes, evaluating our tax positions and establishing deferred tax assets and liabilities. The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax regulations. If the ultimate resolution of uncertainties is different from currently estimated, it could affect income tax expense and the effective tax rate.

Recently Issued Accounting Pronouncements Not Yet Adopted

See Note 2, "Significant Accounting Policies — Recently Issued Accounting Pronouncements Not Yet Adopted" to the consolidated financial statements beginning on page F-10 of this Annual Report.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market Risk

Our exposure to market risk is directly related to our role as investment adviser for separate accounts we manage, funds we offer, and accounts for which we act as sub-investment adviser.

Our revenue for the three years ended December 31, 2017 was generally derived from advisory fees, which are typically based on the market value of our AUM, which can be affected by adverse changes in interest rates, foreign currency exchange rates and equity prices. Accordingly, a decline in the prices of securities would cause our revenue and income to decline, due to a decrease in the value of the assets we manage. In addition, such a decline could cause our clients to withdraw their funds in favor of investments offering higher returns or lower risk, which would cause our revenue and income to decline further.

The value of our AUM was $38.5 billion as of December 31, 2017. A 10% increase or decrease in the value of our AUM, if proportionately distributed over all of our investment strategies, products, and client relationships, would cause an annualized increase or decrease in our revenues of approximately $15.7 million at our current weighted average fee rate excluding the impact of performance fees and fulcrum fee arrangements of 0.408%. There are differences in our fee rates across distribution channels, investment strategies and the size of client relationships. As such, a change in the composition of our AUM, in particular an increase in the proportion of our total assets under management attributable to strategies, clients or relationships with lower effective fee rates, could have a material negative impact on our overall weighted average fee rates and thus different impact to revenues on the same 10% increase or decrease in the value of our AUM.

We are also subject to market risk due to a decline in the value of our holdings and the holdings of our consolidated subsidiaries, which as of December 31, 2017 consist primarily of marketable securities and investments in equity method investees. At December 31, 2017, the aggregate value of our assets subject to market risk was $21.7 million. At December 31, 2017, none of our liabilities were subject to market risk. Assuming a 10% increase or decrease, the fair value of these assets would increase or decrease by $2.2 million, at December 31, 2017.

Exchange Rate Risk

A substantial portion of the accounts that we advise, or sub-advise, hold investments that are denominated in currencies other than the U.S. dollar. Movements in the rate of exchange between the U.S. dollar and the underlying foreign currency affect the values of assets held in accounts that we manage, thereby affecting the amount of revenues we earn. The value of our AUM was $38.5 billion as of December 31, 2017 and approximately 36% of our assets under management across our investment strategies were invested in strategies that primarily invest in securities of non-U.S. companies and approximately 42% of our assets under management were invested in securities denominated in currencies other than the U.S. dollar. To the extent our assets under management are denominated in currencies other than the U.S. dollar, the value of those assets under management will decrease with an increase in the value of the U.S. dollar, or increase with a decrease in the value of the U.S. dollar. Because we believe that many of our clients invest in those strategies in order to gain exposure to non-U.S. currencies, or may implement their own hedging programs, we do not hedge an investment portfolio's exposure to a non-U.S. currency.

TABLE OF CONTENTS

We have not adopted a corporate-level risk management policy to manage this exchange rate risk. Assuming that 42% of our assets under management is invested in securities denominated in currencies other than the U.S. dollar and excluding the impact of any hedging arrangements, a 10% increase or decrease in the value of the U.S. dollar would decrease or increase the fair value of our assets under management by $1.7 billion, which would cause an annualized increase or decrease in revenues of approximately $7.0 million at our current weighted average fee rate excluding the impact of performance fees and fulcrum fee arrangements of 0.408%.

We operate in several foreign countries, but mainly in the United Kingdom. We incur operating expenses and have foreign currency-denominated assets and liabilities associated with these operations, although our revenues are predominately realized in U.S. dollar. We do not believe that foreign currency fluctuations materially affect our results of operations.

Interest Rate Risk

As of December 31, 2017, our $63.4 million in cash was primarily held in demand deposit accounts. As such, interest rate changes would not have a material impact on the income we earn from these deposits. In addition, the Company does not have any debt, and as a result does not have any direct exposure to interest rate risk at December 31, 2017.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our consolidated financial statements and notes thereto begin on page F-5 of this Annual Report and are incorporated herein by reference.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

During the course of their review of our consolidated financial statements as of December 31, 2017, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2017, our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) were effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control system is designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of our financial statements for external purposes in accordance accounting principles generally accepted in the United States of

America. There are inherent limitations in the effectiveness of any internal controls, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurances with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal controls may vary over time.

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has assessed the effectiveness of our internal control over financial reporting as of December 31, 2017. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control — Integrated Framework (2013).

Based on the assessment using those criteria, management concluded that, as of December 31, 2017, our internal control over financial reporting was effective.

TABLE OF CONTENTS

PricewaterhouseCoopers LLP, the independent registered public accounting firm that audited the financial statements included in this Annual Report have issued an audit report on our internal control over financial reporting. This report appears on page F-2 of this Annual Report.

Changes in Internal Control Over Financial Reporting

There have not been any changes in our internal control over financial reporting during the quarter ended December 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

TABLE OF CONTENTS

PART III.
ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this Item is set forth under the proposal “Election of Directors” and under the subheading "Section 16(a) Beneficial Ownership Reporting Compliance" under the heading "Other Matters" in the Company’s 2018 Proxy Statement to be filed with the U.S. Securities and Exchange Commission (“SEC”) within 120 days after December 31, 2017 in connection with the solicitation of proxies for the Company’s 2018 annual meeting of shareholders and is incorporated herein by reference ("Company's 2018 Proxy Statement").

The Company has a code of ethics, “Code of Business Conduct and Ethics,” that applies to all employees, including the Company’s principal executive officer and principal financial officer and principal accounting officer, as well as to the members of the Board of Directors of the Company. The code is available at www.pzena.com. The Company intends to disclose any changes in, or waivers from, this code by posting such information on the same website or by filing a Form 8-K, in each case to the extent such disclosure is required by rules of the SEC or the New York Stock Exchange.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item is set forth under the headings “Executive Compensation” and "2017 Non-Employee Director Compensation" in the Company’s 2018 Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item is set forth under the headings “Security Ownership of Principal Stockholders and Management,” "Equity Compensation Plan Information," "Pzena Investment Management LLC 2006 Equity Incentive Plan," and "Pzena Investment Management, Inc. 2007 Equity Incentive Plan" in the Company’s 2018 Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item is set forth under the heading “Related Party Transactions” and under the subheading “Director Independence” under the proposal "Election of Directors” in the Company’s 2018 Proxy Statement.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item is set forth under the proposal “Ratification of Independent Auditors” in the Company’s 2018 Proxy Statement.

TABLE OF CONTENTS

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

The following documents are filed as part of this Annual Report:

1. Financial Statements

2. Financial Statement Schedules

There are no Financial Statement Schedules filed as part of this Annual Report, since the required information is included in our consolidated financial statements and in the notes thereto.

3. Exhibit List

We have incorporated by reference herein certain exhibits as specified below pursuant to Rule 12b-32 of the Exchange Act. If specific material facts exist which contradict the representations and warranties contained in the documents filed or incorporated by reference in this Annual Report, corrective disclosure has been provided.

Additional information about us may be found elsewhere in this Annual Report, and our other public filings, which are available without charge through the SEC's website at http://www.sec.gov, as well as through our website at www.pzena.com.

Exhibit	Description of Exhibit
3.1	Second Amended and Restated Certificate of Incorporation of Pzena Investment Management, Inc., effective as of May 23, 2017(1)
3.2	Second Amended and Restated Bylaws of Pzena Investment Management, Inc., effective as of January 15, 2016(2)
4.1	Form of Pzena Investment Management, Inc. Class A Common Stock Certificate(3)
4.2	Form of Exchange Rights of Class B Members(3)
4.3	Resale and Registration Rights Agreement, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and the Holders named on the signature pages thereto(4)
4.4	Class B Stockholders' Agreement, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and the Class B Stockholders named on the signature pages thereto(4)
10.1	Amended and Restated Operating Agreement of Pzena Investment Management, LLC, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and the Class B Members named on the signature pages thereto(4)
10.2	Tax Receivable Agreement, dated as of October 30, 2007, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and the Continuing Members and Exiting Members named on the signature pages thereto(4)
10.3	Pzena Investment Management, LLC Amended and Restated 2006 Equity Incentive Plan(5)
10.4	Pzena Investment Management, LLC Amended and Restated Bonus Plan, as amended, dated as of October 21, 2008(6)
10.5	Pzena Investment Management, Inc. 2007 Equity Incentive Plan, as amended, dated as of January 31, 2017(5)
10.6	

	Executive Employment Agreement for Richard S. Pzena, dated as of October 30, 2007, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and Richard S. Pzena[4]
10.7	Executive Employment Agreement for John P. Goetz, dated as of October 30, 2007, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and John P. Goetz[4]

49

TABLE OF CONTENTS

Exhibit	Description of Exhibit
10.8	Amended and Restated Executive Employment Agreement for William L. Lipsey, dated as of October 30, 2007, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and William L. Lipsey(4)
10.9	Indemnification Agreement for Richard S. Pzena, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and Richard S. Pzena(4)
10.10	Indemnification Agreement for Steven M. Galbraith, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and Steven M. Galbraith(4)
10.11	Indemnification Agreement for Joel M. Greenblatt, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and Joel M. Greenblatt(4)
10.12	Indemnification Agreement for Richard P. Meyerowich, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and Richard P. Meyerowich(4)
10.13	Indemnification Agreement for Myron E. Ullman, III, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. and Myron E. Ullman, III(4)
10.14	Indemnification Agreement for Ronald W. Tysoe, dated as of December 11, 2008, by and among Pzena Investment Management, Inc. and Ronald W. Tysoe(7)
10.15	Indemnification Agreement for John P. Goetz, dated as of May 17, 2011, by and among Pzena Investment Management, Inc. and John P. Goetz(8)
10.16	Indemnification Agreement for William L. Lipsey, dated as of May 17, 2011, by and among Pzena Investment Management, Inc. and William L. Lipsey(8)
10.17	Pzena Investment Management, Inc. Non-Employee Director Deferred Compensation Plan, dated as of July 21, 2009 (9)
10.18	Amendment, effective March 24, 2010, to Amended and Restated Operating Agreement of Pzena Investment Management, LLC, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. as the Managing Member of Pzena Investment Management, LLC and those Class B members whose signatures are affixed thereto(10)
10.19	Amendment, dated as of March 5, 2012, to Amended and Restated Operating Agreement of Pzena Investment Management, LLC, dated as of October 30, 2007, by and among Pzena Investment Management, Inc. as the Managing Member of Pzena Investment Management, LLC and those Class B members whose signatures are affixed thereto(8)
10.20	Amendment to Executive Employment Agreement for Richard S. Pzena, dated as of November 1, 2012, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC, and Richard S. Pzena(11)
10.21	Amendment to Executive Employment Agreement for John P. Goetz, dated as of November 1, 2012, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC, and John P. Goetz(11)
10.22	Amendment to Amended and Restated Executive Employment Agreement for William L. Lipsey, dated as of November 1, 2012, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC, and William L. Lipsey(11)
10.23	Amendment, dated as of November 12, 2012, to Tax Receivable Agreement, dated as of October 30, 2007, by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and the Continuing Members and Exiting Members named on the signature pages thereto (12)
10.24	Indemnification Agreement for Charles D. Johnston, dated as of February 5, 2014, by and among Pzena Investment Management, Inc. and Charles D. Johnston (13)
10.25	Lease, dated as of June 13, 2014, between Mutual of America Life Insurance Company, as Landlord and Pzena Investment Management, LLC, as Tenant (14)
10.26	Amendment No. 3 to Pzena Investment Management, LLC Amended and Restated Operating Agreement, dated November 1, 2014 (15)
10.28	Amendment to the Pzena Investment Management, LLC Amended and Restated Bonus Plan, dated December 2, 2014 (15)

10.29	Form of Unit-Based Award Agreement for Phantom Class B Units (15)
10.30	Form of Class B Unit Agreement - Delayed Exchange (15)
10.31	Form of Class B Unit-Based Agreement for Phantom Class B Units - Revised December, 2015 (16)
10.32	Form of Class B Unit Agreement - Delayed Exchange - Revised December, 2015 (16)
10.33	Amended and Restated Agreement of Limited Partnership of Pzena Investment Management, LP, dated as of January 1, 2016(17)
10.34	Form of Class B Unit Option Agreement - Delayed Exchange (filed herewith)

TABLE OF CONTENTS

Exhibit	Description of Exhibit
10.35	Amendment, dated as of December 18, 2017, to Tax Receivable Agreement, dated as of October 30, 2007, as amended by and among Pzena Investment Management, Inc., Pzena Investment Management, LLC and the Continuing Members and Exiting Members named on the signature pages thereto (filed herewith)
14.1	Code of Business Conduct and Ethics, effective as of October 25, 2007, amended as of December 2017 (filed herewith)
14.2	Code of Ethics for Senior Financial Officers(18)
21.1	List of Subsidiaries of Pzena Investment Management, Inc. (filed herewith)
23.1	Consent of PricewaterhouseCoopers LLP, Independent Registered Public Accounting Firm (filed herewith)
23.2	Consent of KPMG LLP, Independent Registered Public Accounting Firm (filed herewith)
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) (filed herewith)
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a) (filed herewith)
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)
101	Materials from the Pzena Investment Management, Inc. Annual Report on Form 10-K for the year ended December 31, 2017, formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Financial Condition, (ii) Consolidated Statements of Operations, (iii) Consolidated Statement of Changes in Equity, (iv) Consolidated Statements of Cash Flows, and (vi) related Unaudited Notes to the Consolidated Financial Statements, tagged in detail (furnished herewith)

(1) Previously filed as an exhibit to our current report on Form 8-K filed with the Securities and Exchange Commission on May 24, 2017 (SEC File No. 001-33761).

(2) Previously filed as an exhibit to our current report on Form 8-K filed with the Securities and Exchange Commission on January 19, 2016 (SEC File No. 001-33761).

(3) Previously filed as an exhibit to Amendment No. 4 of the Registration Statement on Form S-1 (No. 333-143660) of Pzena Investment Management, Inc., which was filed with the Securities and Exchange Commission on October 22, 2007.

(4) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on December 5, 2007 (SEC File No. 001-33761).

(5) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on August 8, 2017 (SEC File No. 001-33761).

(6) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on November 13, 2008 (SEC File No. 001-33761).

(7) Previously filed as an exhibit to our current report on Form 8-K filed with the Securities and Exchange Commission on December 12, 2008 (SEC File No. 001-33761).

(8) Previously filed as an exhibit to our annual report on Form 10-K filed with the Securities and Exchange Commission on March 14, 2012 (SEC File No. 001-33761).

(9) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on November 9, 2009 (SEC File No. 001-33761).

(10) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on May 7, 2010 (SEC File No. 001-33761).

(11) Previously filed as an exhibit to our current report on Form 8-K filed with the Securities and Exchange Commission on November 2, 2012 (SEC File No. 001-33761).

(12) Previously filed as an exhibit to our annual report on Form 10-K filed with the Securities and Exchange Commission on March 13, 2013 (SEC File No. 001-33761).

(13) Previously filed as an exhibit to our current report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2014 (SEC File No. 001-33761).

(14) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on August 7, 2014 (SEC File No. 001-33761).

TABLE OF CONTENTS

(15) Previously filed as an exhibit to our annual report on Form 10-K filed with the Securities and Exchange Commission on March 16, 2015 (SEC File No. 001-33761)

(16) Previously filed as an exhibit to our annual report on Form 10-K filed with the Securities and Exchange Commission on March 14, 2016 (SEC File No. 001-33761).

(17) Previously filed as an exhibit to our quarterly report on Form 10-Q filed with the Securities and Exchange Commission on May 6, 2016 (SEC File No. 001-33761).

(18) Previously filed as an exhibit to our annual report on Form 10-K filed with the Securities and Exchange Commission on March 31, 2008 (SEC File No. 001-33761).

ITEM 16. FORM OF 10-K SUMMARY

None.

TABLE OF CONTENTS

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Pzena Investment Management, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 9, 2018
Pzena Investment Management, Inc.

By: /s/ Richard S. Pzena
Name: Richard S. Pzena
Title: Chief Executive Officer

Each person whose signature appears below constitutes and appoints Jessica R. Doran and Joan F. Berger, and each of them, his or her true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done to effectuate the intent and purpose of this paragraph, as fully as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Pzena Investment Management, Inc. and in the capacities and on the dates indicated.

SIGNATURE	TITLE	DATE
/s/ Richard S. Pzena Richard S. Pzena	Chairman, Chief Executive Officer, Co-Chief Investment Officer (principal executive officer)	March 9, 2018
/s/ Jessica R. Doran Jessica R. Doran	Chief Financial Officer (principal financial and accounting officer)	March 9, 2018
/s/ John P. Goetz John P. Goetz	President, Co-Chief Investment Officer, Director	March 9, 2018
/s/ William L. Lipsey William L. Lipsey	President, Head of Business Development and Client Service, Director	March 9, 2018
/s/ Steven M. Galbraith Steven M. Galbraith	Director	March 9, 2018
/s/ Joel M. Greenblatt Joel M. Greenblatt	Director	March 9, 2018
/s/ Richard P. Meyerowich Richard P. Meyerowich	Director	March 9, 2018
/s/ Charles D. Johnston Charles D. Johnston	Director	March 9, 2018

TABLE OF CONTENTS

INDEX TO FINANCIAL STATEMENTS OF
PZENA INVESTMENT MANAGEMENT, INC.

TABLE OF CONTENTS

Report of Independent Registered Public Accounting Firm
To the Board of Directors and Shareholders of Pzena Investment Management, Inc.,

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated statement of financial condition of Pzena Investment Management, Inc. and its subsidiaries as of December 31, 2017, and the related consolidated statements of operations, comprehensive income, changes in equity and cash flows for the period ended December 31, 2017, including the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017, and the results of their operations and their cash flows for the period ended December 31, 2017 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

TABLE OF CONTENTS

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/PricewaterhouseCoopers LLP
New York, New York
March 9, 2018

We have served as the Company's auditor since 2017.

TABLE OF CONTENTS

Report of Independent Registered Public Accounting Firm
The Board of Directors and Stockholders
Pzena Investment Management, Inc.:

We have audited the accompanying consolidated statement of financial condition of Pzena Investment Management, Inc. (the Company) as of December 31, 2016, and the related consolidated statements of operations, comprehensive income, changes in equity, and cash flows for the years ended December 31, 2016 and 2015. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Pzena Investment Management, Inc. as of December 31, 2016, and the results of its operations and its cash flows for the years ended December 31, 2016 and 2015, in conformity with U.S. generally accepted accounting principles.

/s/KPMG LLP
New York, New York
March 10, 2017

TABLE OF CONTENTS

PZENA INVESTMENT MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(in thousands, except share and per-share amounts)

	As of December 31, 2017	December 31, 2016
ASSETS		
Cash ($3,717 and $3,258)[1]	$63,414	$ 43,522
Restricted Cash	1,017	3,636
Due from Broker ($1,485 and $0)[1]	1,875	842
Advisory Fees Receivable	32,531	26,326
Investments in Marketable Securities, at Fair Value ($3,589 and $3,174)[1]	5,452	14,323
Equity Method Investments ($338 and $0)[1]	16,285	7,987
Receivable from Related Parties	1,453	1,008
Other Receivables ($15 and $9)[1]	132	302
Prepaid Expenses and Other Assets	990	769
Deferred Tax Assets	39,639	73,441
Property and Equipment, Net of Accumulated Depreciation of $3,063 and $2,260, respectively	6,259	6,965
TOTAL ASSETS	$169,047	$ 179,121
LIABILITIES AND EQUITY		
Liabilities:		
Accounts Payable and Accrued Expenses ($14 and $18)[1]	$31,983	$ 24,648
Due to Broker ($0 and $3)[1]	144	17
Securities Sold Short, at Fair Value	—	2,622
Liability to Selling and Converting Shareholders	36,441	65,485
Deferred Compensation Liability	918	4,157
Other Liabilities	272	858
TOTAL LIABILITIES	69,758	97,787
Commitments and Contingencies (see Note 12)		
Equity:		
Preferred Stock (Par Value $0.01; 200,000,000 Shares Authorized; None Outstanding)	—	—
Class A Common Stock (Par Value $0.01; 750,000,000 Shares Authorized; 18,096,554 and 17,340,090 Shares Issued and Outstanding in 2017 and 2016, respectively)	180	173
Class B Common Stock (Par Value $0.000001; 750,000,000 Shares Authorized; 50,709,673 and 50,461,598 Shares Issued and Outstanding in 2017 and 2016 respectively)	—	—
Additional Paid-In Capital	7,915	5,996
Retained Earnings	24,214	22,349
Accumulated Other Comprehensive Loss	(5)	(25)
Total Pzena Investment Management, Inc.'s Equity	32,304	28,493
Non-Controlling Interests	66,985	52,841
TOTAL EQUITY	99,289	81,334
TOTAL LIABILITIES AND EQUITY	$169,047	$ 179,121

1 Asset and liability amounts in parentheses represent the aggregated balances at December 31, 2017 and December 31, 2016 attributable to Pzena International Value Service (a series of Pzena Investment Management International, LLC) and Pzena Investment Management Special Situations, LLC, which were variable interest entities as of December 31, 2017 and December 31, 2016, respectively. Aggregated balances of variable interest entities at

December 31, 2017 also reflect Pzena U.S. Best Ideas (GP), LLC.

See accompanying notes to consolidated financial statements.

TABLE OF CONTENTS

PZENA INVESTMENT MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except share and per-share amounts)

	For the Years Ended December 31,		
	2017	2016	2015
REVENUE	$141,295	$108,336	$116,607
EXPENSES			
Compensation and Benefits Expenses	58,904	48,330	46,523
General and Administrative Expenses	13,337	12,788	14,667
TOTAL OPERATING EXPENSES	72,241	61,118	61,190
Operating Income	69,054	47,218	55,417
OTHER INCOME/ (EXPENSE)			
Interest Income	213	80	40
Interest Expense	(29)	(24)	(21)
Dividend Income	368	313	734
Net Realized and Unrealized Gains/ (Losses) from Investments	2,600	1,776	(3,235)
Equity in the Earnings/ (Losses) of Affiliates	1,517	1,243	(109)
Change in Liability to Selling and Converting Shareholders	20,819	(51,442)	(423)
Other Income/ (Expense)	120	12	(286)
Total Other Income/ (Expense)	25,608	(48,042)	(3,300)
Income Before Income Taxes	94,662	(824)	52,117
Income Tax Expense/ (Benefit)	34,512	(54,475)	5,114
Net Income	60,150	53,651	47,003
Less: Net Income Attributable to Non-Controlling Interests	53,242	37,472	39,324
Net Income Attributable to Pzena Investment Management, Inc.	$6,908	$16,179	$7,679
Net Income for Basic Earnings per Share	$6,908	$16,179	$7,679
Basic Earnings per Share	$0.40	$1.01	$0.55
Basic Weighted Average Shares Outstanding	17,338,348	15,962,902	14,014,219
Net Income for Diluted Earnings per Share	$40,064	$39,600	$33,809
Diluted Earnings per Share[1]	$0.40	$0.58	$0.50
Diluted Weighted Average Shares Outstanding[2]	70,934,362	68,849,172	68,126,786
Cash Dividends per Share of Class A Common Stock	$0.37	$0.41	$0.41

1 During the year-ended ended December 31, 2017, the calculation of diluted earnings per share resulted in an increase in earnings per share. Therefore, diluted earnings per share is assumed to be equal to basic earnings per share. Please refer to Note 5, "Earnings per Share," for further details.

2 The Company issues restricted share of Class A common stock and restricted Class B units that have non-forfeitable dividend rights. Under the “two-class method,” these shares and units are considered participating securities and are required to be included in the computation of diluted earnings per share.

See accompanying notes to consolidated financial statements.

TABLE OF CONTENTS

PZENA INVESTMENT MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)

	For the Years Ended December 31,		
	2017	2016	2015
NET INCOME	$60,150	$53,651	$47,003
OTHER COMPREHENSIVE INCOME/ (LOSS)			
Foreign Currency Translation Adjustment	122	(93)	(10)
Total Other Comprehensive Income/ (Loss)	122	(93)	(10)
Comprehensive Income	60,272	53,558	46,993
Less: Comprehensive Income Attributable to Non-Controlling Interests	53,344	37,402	39,316
Total Comprehensive Income Attributable to Pzena Investment Management, Inc.	$6,928	$16,156	$7,677

See accompanying notes to consolidated financial statements.

TABLE OF CONTENTS

PZENA INVESTMENT MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(in thousands, except share and per-share amounts)

	Shares of Class A Common Stock	Shares of Class B Common Stock	Class A Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Non-Controlling Interests	Total
Balance at December 31, 2014	13,044,719	52,891,939	$ 130	$ 8,007	$ —	$ 10,264	$ 66,632	$ 85,033
Unit Conversion	2,772,171	(2,772,171)	28	2,745	—	—	(2,278)	495
Amortization of Non-Cash Compensation	29,677	1,510,626	—	1,848	—	—	6,344	8,192
Sale of Shares Under Equity Incentive Plan	—	78,093	—	87	—	—	285	372
Non-Cash Compensation Modification	—	(142,315)	—	(141)	—	—	(572)	(713)
Directors' Shares	—	—	—	82	—	—	310	392
Net Income	—	—	—	—	—	7,679	39,324	47,003
Foreign Currency Translation Adjustments	—	—	—	—	(2)	—	(8)	(10)
Options Exercised	962	715,706	—	333	—	—	1,355	1,688
Repurchase and Retirement of Class A Common Stock	(629,174)	—	(6)	(5,770)	—	—	—	(5,776)
Repurchase and Retirement of Class B Units	—	(192,406)	—	(407)	—	—	(1,619)	(2,026)
Contributions from Non-Controlling Interests	—	—	—	—	—	—	597	597
Distributions to Non-Controlling Interests	—	—	—	—	—	—	(44,295)	(44,295)
Class A Cash Dividends Declared and Paid ($0.41 per share)	—	—	—	—	—	(5,490)	—	(5,490)
Other	—	—	—	(965)	—	—	965	—
Balance at December 31, 2015	15,218,355	52,089,472	$ 152	$ 5,819	$ (2)	$ 12,453	$ 67,040	$ 85,462
Adjustment for the Cumulative Effect of Applying ASU 2015-02	—	—	—	—	—	—	(10,835)	(10,835)
Adjusted Balance at January 1, 2016	15,218,355	52,089,472	152	5,819	(2)	12,453	56,205	74,627
Unit Conversion	2,426,740	(2,426,740)	24	2,382	—	—	(2,050)	356
Amortization of Non-Cash Compensation	34,934	501,644	—	693	—	—	2,065	2,758
Sale of Shares Under Equity Incentive Plan	—	87,563	—	97	—	—	304	401
Directors' Shares	—	—	—	111	—	—	364	475
Net Income	—	—	—	—	—	16,179	37,472	53,651

Foreign Currency Translation Adjustments	—	—	—	—	(23)	—	(70)	(93)
Options Exercised	—	282,519	—	220	—	—	675	895
Repurchase and Retirement of Class A Common Stock	(339,939)	—	(3)	(2,676)	—	—	—	(2,679)
Repurchase and Retirement of Class B Units	—	(72,860)	—	(190)	—	—	(584)	(774)
Contributions from Non-Controlling Interests	—	—	—	—	—	—	1,139	1,139
Distributions to Non-Controlling Interests	—	—	—	—	—	—	(43,059)	(43,059)
Class A Cash Dividends Declared and Paid ($0.41 per share)	—	—	—	—	—	(6,283)	—	(6,283)
Effect of Deconsolidation	—	—	—	—	—		(80)	(80)
Other	—	—	—	(460)	—	—	460	—
Balance at December 31, 2016	17,340,090	50,461,598	$ 173	$ 5,996	$ (25)	$ 22,349	$ 52,841	$ 81,334
Adjustment for the Cumulative Effect of Applying ASU 2016-09	—	—	—	—	—	1,377	—	1,377
Adjusted Balance at January 1, 2017	17,340,090	50,461,598	173	5,996	(25)	23,726	52,841	82,711
Unit Conversion	855,535	(855,535)	9	1,600	—	—	(1,059)	550
Amortization of Non-Cash Compensation	34,934	443,198	—	1,070	—	—	3,092	4,162
Issuance of Shares under Equity Incentive Plan	—	620,543	—	1,118	—	—	3,295	4,413
Sale of Shares Under Equity Incentive Plan	—	31,803	—	51	—	—	153	204
Directors' Shares	—	—	—	121	—	—	360	481
Net Income	—	—	—	—	—	6,908	53,242	60,150
Foreign Currency Translation Adjustments	—	—	—	—	20	—	102	122
Options Exercised	16,722	41,781	—	—	—	—	—	—
Repurchase and Retirement of Class A Common Stock	(150,727)	—	(2)	(1,488)	—	—	—	(1,490)
Repurchase and Retirement of Class B Units	—	(33,715)	—	(96)	—	—	(278)	(374)
Contributions from Non-Controlling Interests	—	—	—	—	—	—	4,166	4,166
Distributions to Non-Controlling Interests	—	—	—	—	—	—	(44,095)	(44,095)
Class A Cash Dividends Declared and Paid ($0.37 per share)	—	—	—	—	—	(6,420)	—	(6,420)
Effect of Deconsolidation	—	—	—	—	—	—	(5,291)	(5,291)

Other	—	—	—	(457)	—	—	457	—
Balance at December 31, 2017	18,096,554	50,709,673	$ 180	$ 7,915	$ (5)	$ 24,214	$ 66,985	$ 99,289

See accompanying notes to consolidated financial statements.

TABLE OF CONTENTS

PZENA INVESTMENT MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For the Years Ended December 31,		
	2017	2016	2015
OPERATING ACTIVITIES			
Net Income	$60,150	$53,651	$47,003
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Depreciation	1,024	1,058	789
Loss on Disposal of Fixed Assets	6	—	428
Non-Cash Compensation	10,182	6,933	11,092
Directors' Share Grants	481	475	392
Net Realized and Unrealized (Gains)/ Losses from Investments	(2,600)	(1,776)	3,235
Equity in the (Earnings)/ Losses of Affiliates	(1,517)	(1,243)	109
Non-Cash Performance Fees	(237)	—	—
Foreign Currency Translation Adjustment	122	(93)	(10)
Lease Liability	—	—	862
Change in Liability to Selling and Converting Shareholders	(26,427)	51,442	423
Deferred Income Taxes	37,269	(56,058)	2,910
Changes in Operating Assets and Liabilities:			
Advisory Fees Receivable	(6,205)	(4,079)	691
Due from Broker	(1,026)	(581)	(198)
Restricted Cash	(1,222)	(84)	(742)
Prepaid Expenses and Other Assets	(60)	235	69
Non-Cash Compensation Modification	—	—	(713)
Due to Broker	127	(20)	(668)
Accounts Payable, Accrued Expenses, and Other Liabilities	2,566	14,064	(214)
Tax Receivable Agreement Payments	(4,155)	(3,050)	(3,512)
Change in Lease Liability	—	—	(1,216)
Purchases of Investments	(41,077)	(28,831)	(40,493)
Proceeds from Sale of Investments	40,329	26,529	37,193
Net Cash Provided by Operating Activities	67,730	58,572	57,430
INVESTING ACTIVITIES			
Purchases of Investments	(869)	(2,159)	(8,669)
Proceeds from Sale of Investments	2,180	2,428	9,772
Payments (to)/ from Related Parties	(445)	46	(947)
Purchase of Property and Equipment	(324)	(120)	(6,348)
Net Cash Provided by/ (Used in) Investing Activities	542	195	(6,192)
FINANCING ACTIVITIES			
Repurchase and Retirement of Class A Common Stock	(1,490)	(2,679)	(5,776)
Repurchase and Retirement of Class B Units	(374)	(774)	(2,026)
Option Exercise	—	895	1,688
Sale of Shares under Equity Incentive Plan	204	401	372
Distributions to Non-Controlling Interests	(44,095)	(43,059)	(44,295)
Contributions from Non-Controlling Interests	4,166	1,139	597
Dividends	(6,420)	(6,283)	(5,490)
Net Cash Used in Financing Activities	(48,009)	(50,360)	(54,930)
NET CHANGE IN CASH	$20,263	$8,407	$(3,692)

CASH — Beginning of Year	$43,522	$35,417	$39,109
Adjustment for the Cumulative Effect of Applying ASU 2015-02 for the Deconsolidation of a Legal Entity	—	(227)	—
Effect of Deconsolidation of Affiliates	(371)	(75)	—
Net Change in Cash	20,263	8,407	(3,692)
CASH — End of Year	$63,414	$43,522	$35,417
Supplementary Cash Flow Information:			
Unit Conversion	$550	$356	$495
Issuance of Shares under Equity Incentive Plan	$4,413	$—	$—
Income Taxes Paid	$797	$665	$1,031

See accompanying notes to consolidated financial statements.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements
Note 1 — Organization

Pzena Investment Management, Inc. (the "Company") functions as the sole managing member of its operating company, Pzena Investment Management, LLC (the "operating company"). As a result, the Company: (i) consolidates the financial results of the operating company and reflects the membership interests that it does not own as a non-controlling interest in its consolidated financial statements; and (ii) recognizes income generated from its economic interest in the operating company's net income.

The operating company is an investment adviser which is registered under the Investment Advisers Act of 1940 and is headquartered in New York, New York. As of December 31, 2017, the operating company managed assets in a variety of value-oriented investment strategies across a wide range of market capitalizations in both U.S. and non-U.S. capital markets.

The Company also serves as the general partner of Pzena Investment Management, LP, a partnership formed with the objective of aggregating employee ownership in the operating company into one entity.

The Company has consolidated the results of operations and financial condition of the following entities as of December 31, 2017:

Legal Entity	Type of Entity (Date of Formation)	Ownership at December 31, 2017	
Pzena Investment Management, Pty	Australian Proprietary Limited Company (12/16/2009)	100.0	%
Pzena Financial Services, LLC	Delaware Limited Liability Company (10/15/2013)	100.0	%
Pzena Investment Management, LTD	England and Wales Private Limited Company (1/08/2015)	100.0	%
Pzena U.S. Best Ideas (GP), LLC	Delaware Limited Liability Company (11/16/2017)	100.0	%
Pzena Investment Management Special Situations, LLC	Delaware Limited Liability Company (12/01/2010)	99.9	%
Pzena International Value Service, a series of the Pzena Investment Management International, LLC	Delaware Limited Liability Company (12/22/2003)	67.2	%

Note 2 — Significant Accounting Policies

Basis of Presentation:

The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") and related Securities and Exchange Commission ("SEC") rules and regulations.

Principles of Consolidation:

The Company's policy is to consolidate those entities in which it has a direct or indirect controlling financial interest based on either the voting interest model or the variable interest model. As such, the Company consolidates majority-owned subsidiaries in which it has a controlling financial interest, and certain investment vehicles the operating company sponsors for which it is the investment adviser that are considered to be variable-interest entities (“VIEs”), and for which the Company is deemed to be the primary beneficiary.

Pursuant to the Consolidation Topic of the FASB Accounting Standards Codification ("FASB ASC"), for legal entities evaluated for consolidation, the Company determines whether interests it holds and fees paid to it qualify as a variable interest. If it is determined that the Company does not have a variable interest in the entity, no further analysis is required and the Company does not consolidate the entity. If it is determined that the Company has a variable interest, it considers its direct economic interests and the proportionate indirect interests through related parties to determine if it is the primary beneficiary of the VIE.

For equity investments where the Company does not control the investee, and where it is not the primary beneficiary of a VIE, but can exert significant influence over the financial and operating policies of the investee, the Company follows the equity method of accounting. The evaluation of whether the Company exerts control or significant influence over the financial and operating policies of the investee requires significant judgment based on the facts and circumstances surrounding each investment. Factors considered in these evaluations may include the type of investment, the legal structure of the investee, the terms of the investment agreement, or other agreements with the investee.

TABLE OF CONTENTS
Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 2 — Significant Accounting Policies (Continued)

The Company analyzes entities structured as series funds which comply with the requirements included in the Investment Company Act of 1940 for registered mutual funds as voting interest entities because the shareholders are deemed to have the ability to direct the activities of the fund that most significantly impact the fund's economic performance.

Consolidated Entities

The Company consolidates the financial results of the operating company and records in its own equity its pro-rata share of transactions that impact the operating company’s net equity, including unit and option issuances, repurchases, and retirements. The operating company’s pro-rata share of such transactions are recorded as an adjustment to additional paid-in capital or non-controlling interests, as applicable, on the consolidated statements of financial condition.

The majority-owned subsidiaries in which the Company, through its interest in the operating company, has a controlling financial interest and the VIEs for which the Company is deemed to be the primary beneficiary are collectively referred to as “consolidated subsidiaries.” Non-controlling interests recorded on the consolidated financial statements of the Company include the non-controlling interests of the outside investors in each of these entities, as well as those of the operating company. All significant inter-company transactions and balances have been eliminated through consolidation.

During 2014, the Company provided the initial cash investment for three Pzena mutual funds in an effort to generate an investment performance track record to attract third-party investors. During 2016, the Company provided the initial cash investment for the launch of a fourth Pzena mutual fund: the Pzena Small Cap Value Fund. Due to their series fund structure, registration, and compliance with the requirements of the Investment Company Act of 1940, these funds are analyzed for consolidation under the voting interest model. As a result of the Company's initial interests, it consolidated the Pzena Mid Cap Value Fund, Pzena Long/Short Value Fund, and Pzena Small Cap Value Fund. On July 11, 2016, due to additional subscriptions into the Pzena Small Cap Value Fund, the Company's ownership decreased to 36.1%. On November 9, 2017 and December 21, 2017 due to additional subscriptions into the Pzena Mid Cap Value Fund and Pzena Long/Short Value Fund, respectively, the Company's ownership decreased to 41.7% and 35.5%, respectively. As the Company was no longer deemed to control the funds, it deconsolidated the entities, removed the related assets, liabilities and non-controlling interest from its balance sheet and classified the Company's remaining investments as an equity method investments.

The operating company is the managing member of Pzena International Value Service, a series of Pzena Investment Management International, LLC. The operating company is considered the primary beneficiary of this entity. At December 31, 2017, Pzena International Value Service’s $5.2 million in net assets were included in the Company’s consolidated statements of financial condition.

These consolidated investment partnerships are investment companies and apply specialized industry accounting for investment companies. The Company has retained this specialized accounting for these investment partnerships pursuant to U.S. GAAP.

Non-Consolidated Variable Interest Entities

VIEs that are not consolidated continue to receive investment management services from the operating company and are generally private investment partnerships sponsored by the operating company. The total net assets of these VIEs was approximately $165.5 million and $44.3 million at December 31, 2017 and December 31, 2016, respectively.

As of December 31, 2017 and December 31, 2016, in order to satisfy certain of the Company's obligations under its deferred compensation programs, the operating company had $3.0 million and $3.2 million in investments, respectively, in certain of these firm-sponsored vehicles, for which the Company was not deemed to be the primary beneficiary. The Company's exposure to risk in the non-consolidated VIEs is generally limited to any equity investment and any uncollected management fees. As of December 31, 2017 and December 31, 2016, the Company's maximum exposure to loss as a result of its involvement with the non-consolidated VIEs was $3.2 million and $3.3 million, respectively.

TABLE OF CONTENTS
Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 2 — Significant Accounting Policies (Continued)

Accounting Pronouncements Adopted in 2017:

In March 2016, the FASB issued ASU No. 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting." The Company adopted ASU No. 2016-09 as of January 1, 2017. This standard requires excess tax benefits and tax deficiencies to be recorded in the consolidated statements of operations as a component of Income Tax Expense when equity awards vest or are settled. The Company is no longer required to delay recognition of an excess tax benefit until it reduces current taxes payable. The standard also requires excess tax benefits to be classified as operating activities along with other income tax cash flows within the consolidated statements of cash flows. In addition, ASU No. 2016-09 allows entities to make an accounting policy election to either estimate the number of forfeitures expected to occur, as was previously required, or to account for actual forfeitures as they occur. The Company has elected to account for forfeitures as they occur, rather than estimate expected forfeitures. The adoption of ASU No. 2016-09 resulted in a net cumulative effect adjustment reflecting a $1.4 million increase to retained earnings and the deferred tax asset as of January 1, 2017, related to the recognition of the previously unrecognized excess tax benefits using the modified retrospective method. Estimates of forfeitures in prior periods were immaterial, and therefore are not included in the cumulative effect adjustment. The amendments related to the classification of the excess tax benefits in the consolidated statements of cash flows were adopted on a prospective basis, which did not require the restatement of prior periods.

Management’s Use of Estimates:

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses for the period. Actual results could materially differ from those estimates.

Revenue Recognition:

Revenue, comprised of advisory fee income, is recognized over the period in which advisory services are provided. Advisory fee income includes management fees that are calculated based on percentages of assets under management (“AUM”), generally billed quarterly, either in arrears or advance, depending on their contractual terms. Advisory fee income also includes performance fees that may be earned by the Company depending on the investment return of AUM, as well as fulcrum fee arrangements. Performance fee arrangements generally entitle the Company to participate, on a fixed-percentage basis, in any returns generated in excess of an agreed-upon benchmark. The Company’s participation percentage in such return differentials is then multiplied by AUM to determine the performance fees earned. In general, returns are calculated on an annualized basis over the contract’s measurement period, which usually extends to three years. Performance fees are generally payable annually or quarterly. Fulcrum fee arrangements require a reduction in the base fee, or allow for a performance fee if the relevant investment strategy underperforms or outperforms, respectively, the agreed-upon benchmark over the contract's measurement period, which extends to three years. Fulcrum fees are generally payable quarterly. Following the preferred method identified in the Revenue Recognition Topic of the FASB ASC, fee income is recorded at the conclusion of the contractual performance period, when all contingencies are resolved. For the years ended December 31, 2017, 2016, and 2015, the Company recognized approximately $3.2 million, $0.2 million and $4.5 million, respectively, in performance fee income. For the year ended December 31, 2016, the Company recognized a $1.0 million reduction in base fees related to fulcrum fee arrangements. For the years ended December 31, 2017 and 2015, the Company did not recognize a reduction in base fees related to fulcrum fee arrangements.

Cash:

At December 31, 2017 and 2016, cash was $63.4 million and $43.5 million, respectively. The Company maintains its cash in bank deposit and other accounts whose balances often exceed federally insured limits. Cash is stated at cost, which approximates fair value.

Interest on cash is recorded as Interest Income on an accrual basis in the consolidated statements of operations.

Restricted Cash:

The Company maintained $1.0 million and $3.6 million at December 31, 2017, and 2016, respectively, of compensating balances recorded in Restricted Cash in the consolidated statements of financial condition.

Included in this balance at December 31, 2017 and 2016 is a $1.0 million letter of credit issued by a third party in lieu of a cash security deposit, as required by the Company's lease for its current and former corporate headquarters.

Also included in these balances at December 31, 2016, were amounts of cash collateral for margin accounts established by the Pzena Long/Short Value Fund required to maintain to support securities sold short, not yet purchased of $2.6 million. On December 21, 2017, the Pzena Long/Short Value Fund was deconsolidated from the Company's consolidated statement of financial condition.

Due to/from Broker:

Due to/from Broker consists primarily of amounts payable/receivable for unsettled securities transactions held/initiated at the clearing brokers of the Company and its consolidated subsidiaries.

Non-Cash Compensation:

All non-cash compensation awards granted have varying vesting schedules and are issued at prices equal to the assessed fair market value at the time of issuance. Expenses associated with these awards are recognized over the period during which employees are required to provide service. The Company accounts for forfeitures as they occur.

Investments:

Investment securities, trading

Investments classified as trading securities consist of equity securities held by the Company and its consolidated subsidiaries. Certain of the Company's investments are held to satisfy the Company's obligations under its deferred compensation program. Dividends associated with the Company's investments and the investments of the Company's consolidated subsidiaries are recognized as dividend income on an ex-dividend basis in the consolidated statements of operations.

Securities Sold Short represents securities sold short, not yet purchased by the Pzena Long/Short Value Fund, which was consolidated with the Company's financial statements through December 21, 2017. On December 21, 2017, the Pzena Long/Short Value Fund was deconsolidated from the Company's consolidated statement of financial condition due to additional subscriptions into the fund. Dividend expense associated with these investments is reflected in Other Income/ (Expense) on an ex-dividend basis in the consolidated statements of operations.

All such investments are recorded at fair value, with net realized and unrealized gains and losses recognized as a component of Net Realized and Unrealized Gains/ (Losses) from Investments in the consolidated statements of operations.

Investments in equity method investees

The Company accounts for its investments in certain private investment partnerships in which the Company has non-controlling interests and exercises significant influence, using the equity method. These investments are included in Equity Method Investments in the Company's consolidated statements of financial condition. The carrying value of these investments are recorded at the amount of capital reported by the private investment partnership or mutual fund.

The capital account reflects any contributions paid to, distributions received from, and equity earnings of, the entities. The earnings of these investments are recognized in Equity in Earnings/ (Losses) of Affiliates in the consolidated statements of operations.

Investments in equity method investees are evaluated for impairment as events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. If the carrying amounts of the assets exceed their respective fair values, additional impairment tests are performed to measure the amounts of impairment losses, if any. For the years ended December 31, 2017, 2016, and 2015, no impairment losses were recognized.

TABLE OF CONTENTS
Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 2 — Significant Accounting Policies (Continued)

Securities Valuation:

Investments in equity securities and securities sold short for which market quotations are available are valued at the last reported price or closing price on the primary market or exchange on which they trade. If no reported equity sales occurred on the valuation date, equity investments are valued at the bid price. Transactions are recorded on a trade date basis.

The net realized gain or loss on sales of equity securities and securities sold short is determined on a specific identification basis and is included in Net Realized and Unrealized Gains/ (Losses) from Investments in the consolidated statements of operations.

Concentrations of Credit Risk:

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash, amounts due from brokers, and advisory fees receivable. The Company maintains its cash in bank deposits and other accounts whose balances often exceed federally insured limits.

The concentration of credit risk with respect to advisory fees receivable is generally limited due to the short payment terms extended to clients by the Company. On a periodic basis, the Company evaluates its advisory fees receivable and establishes an allowance for doubtful accounts, if necessary, based on a history of past write-offs, collections, and current credit conditions. For the year ended December 31, 2017 and 2016, approximately 11.3% and 10.1%, respectively, of the Company's advisory fees were generated from advisory agreements with one client relationship. At December 31, 2017 and 2016, no allowance for doubtful accounts has been deemed necessary.

Property and Equipment:

Property and equipment is carried at cost, less accumulated depreciation and amortization. Depreciation is provided on a straight-line basis over the estimated useful lives of the respective assets, which range from three to seven years. Leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvements or the remaining lease term.

Business Segments:

The Company views its operations as comprising one operating segment.

Income Taxes:

The Company is a “C” corporation under the Internal Revenue Code, and is thus liable for federal, state, and local taxes on the income derived from its economic interest in its operating company. The operating company is a limited liability company that has elected to be treated as a partnership for tax purposes. It has not made a provision for federal or state income taxes because it is the individual responsibility of each of the operating company’s members (including the Company) to separately report their proportionate share of the operating company’s taxable income or loss. The operating company has made a provision for New York City Unincorporated Business Tax (“UBT”) and its consolidated subsidiary Pzena Investment Management, LTD has made a provision for U.K. income taxes.

Judgment is required in evaluating the Company's uncertain tax positions and determining its provision for income taxes. The Company establishes reserves for tax-related uncertainties based on estimates of whether, and the extent to which, additional taxes will be due. These liabilities are established when the Company believes that certain positions might be challenged despite its belief that its tax return positions are in accordance with applicable tax laws. The Company adjusts these liabilities in light of changing facts and circumstances, such as the closing of a tax audit, new tax legislation, or the change of an estimate. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will affect the provision for income taxes in the period in which such determination is made. The provision for income taxes includes the effect of reserve provisions and changes to reserves that are considered appropriate. It is also the Company’s policy to recognize accrued interest, and penalties associated with uncertain tax positions in Income Tax Expense/ (Benefit) on the consolidated statements of operations.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 2 — Significant Accounting Policies (Continued)

The Company and its consolidated subsidiaries account for all U.S. federal, state, local and U.K. taxation pursuant to the asset and liability method, which requires deferred income tax assets and liabilities to be recorded for temporary differences between the carrying amount and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future, based on enacted tax laws and rates applicable to the periods in which the temporary differences are expected to affect taxable income.

The Company's purchase of membership units of the operating company concurrent with the initial public offering, and the subsequent and future exchanges by holders of Class B units of the operating company for shares of Class A common stock (pursuant to the exchange rights provided for in the operating company's operating agreement), has resulted in, and is expected to continue to result in, increases in the Company's share of the tax basis of the tangible and intangible assets of the operating company, which will increase the tax depreciation and amortization deductions that otherwise would not have been available to the Company. These increases in tax basis and tax depreciation and amortization deductions have reduced, and are expected to continue to reduce, the amount of cash taxes that the Company would otherwise be required to pay in the future. The Company has entered into a tax receivable agreement with past, current, and future members of the operating company that requires the Company to pay to any member involved in any exchange transaction 85% of the amount of cash tax savings, if any, in U.S. federal, state and local income tax or foreign or franchise tax that it realizes as a result of these increases in tax basis and, in limited cases, transfers or prior increases in tax basis. The Company expects to benefit from the remaining 15% of cash tax savings, if any, in income tax it realizes. Payments under the tax receivable agreement will be based on the tax reporting positions that the Company will determine. The Company will not be reimbursed for any payments previously made under the tax receivable agreement if a tax basis increase is successfully challenged by the Internal Revenue Service.

The Company records an increase in deferred tax assets for the estimated income tax effects of the increases in tax basis based on enacted federal and state tax rates at the date of the exchange. The Company records 85% of the estimated realizable tax benefit (which is the recorded deferred tax asset less any recorded valuation allowance) as an increase to the liability due under the tax receivable agreement, which is reflected as the liability to selling and converting shareholders in the accompanying consolidated financial statements. The remaining 15% of the estimated realizable tax benefit is initially recorded as an increase to the Company's additional paid-in capital. All of the effects to the deferred tax asset of changes in any of the estimates after the tax year of the exchange will be reflected in the provision for income taxes. Similarly, the effect of subsequent changes in the enacted tax rates will be reflected in the provision for income taxes.

Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount that is more-likely-than-not to be realized. At December 31, 2017 and 2016, the Company did not have a valuation allowance recorded against its deferred tax assets.

The income tax expense, or benefit, is the tax payable or refundable for the period, plus or minus the change during the period in deferred tax assets and liabilities. The Company records its deferred tax liabilities as a component of other liabilities in the consolidated statements of financial condition.

Upon adoption of ASU No. 2016-09 as of January 1, 2017, all excess tax benefits or tax deficiencies related to stock- and unit-transactions are reflected in the consolidated statements of operations as a component of the provision for income taxes. Previously, these excess tax benefits were not recognized until they resulted in a reduction of cash taxes payable, and were subsequently recorded in equity when they reduced cash taxes payable. The Company only recognized a tax benefit from stock- and unit-based awards in Additional Paid-In Capital if an incremental tax benefit was realized after all other tax benefits available had been utilized. The adoption of ASU No. 2016-09 resulted in a net cumulative effect adjustment reflecting a $1.4 million increase to retained earnings and the deferred tax asset as of January 1, 2017, related to the recognition of the previously unrecognized excess tax benefits using the modified retrospective method.

Foreign Currency:

The functional currency of the Company is the U.S. Dollar. Assets and liabilities of foreign operations whose functional currency is not the U.S. Dollar are translated at the exchange rate in effect at the applicable reporting date, and the consolidated statements of operations are translated at the average exchange rates in effect during the applicable period. A charge or credit is recorded to other comprehensive income/ (loss) to reflect the translation of these amounts to the extent the non-U.S. currency is designated the functional currency of the subsidiary. Non-functional currency related transaction gains and losses are immediately recorded in the consolidated statements of operations. For the year ended December 31, 2017, the Company recorded $0.1 million of other comprehensive income associated with foreign currency translation adjustments. For both the years ended December 31, 2016 and 2015, the Company recorded approximately $0.1 million of other comprehensive loss associated with foreign currency translation adjustments.

Investment securities and other assets and liabilities denominated in foreign currencies are remeasured into U.S. Dollar amounts at the date of valuation. Purchases and sales of investment securities, and income and expense items denominated in foreign currencies, are remeasured into U.S. Dollar amounts on the respective dates of such transactions.

The Company does not isolate the portion of the results of its operations resulting from the impact of fluctuations in foreign exchange rates on its non-U.S. investments. Such fluctuations are included in Net Realized and Unrealized Gains/ (Losses) from Investments in the consolidated statements of operations.

Reported net realized foreign exchange gains or losses arise from sales of foreign currencies, currency gains or losses realized between the trade and settlement dates on securities transactions, and the difference between the amounts of dividends, interest, foreign withholding taxes, and other receivables and payables recorded on the Company’s consolidated statements of financial condition and the U.S. Dollar equivalent of the amounts actually received or paid. Net unrealized foreign exchange gains and losses arise from changes in the fair values of assets and liabilities resulting from changes in exchange rates.

Recently Issued Accounting Pronouncements Not Yet Adopted:

In November 2016, the FASB issued ASU No. 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash." This update requires entities to show the changes in the total cash, cash equivalents, restricted cash, and restricted cash equivalents in the statement of cash flows. This guidance is effective for the fiscal years and interim periods within those years beginning after December 15, 2017. The guidance should be applied using a retrospective approach. Upon adoption, the net change in cash presented in the consolidated statement of cash flows will reflect the total of cash, cash equivalents, and restricted cash.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230)." This update provides specific guidance on cash flow classification issues, which is intended to reduce the diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The guidance is effective for the fiscal years and interim periods within those years beginning after December 15, 2017. The guidance should be applied using a modified retrospective approach. The Company does not expect the standard to have a material impact on the consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments - Credit Losses (Topic 326)." This new guidance requires the use of an “expected loss” model, rather than an “incurred loss” model, for financial instruments measured at amortized cost and also requires companies to record allowances for available-for-sale debt securities rather than reduce the carrying amount. The guidance is effective for the fiscal years and interim periods within those years beginning after December 15, 2019. The guidance should be applied using a retrospective approach. The Company is currently assessing the impact of this standard, however, does not expect the standard to have a material impact on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." This amended standard was written to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The new standard requires lessees to recognize a right-of-use asset and lease liability for all leases with terms of more than 12 months. Recognition, measurement and presentation of expenses will depend on classification as a finance or operating lease. The amendments also require certain quantitative and qualitative disclosure. Accounting guidance for lessors is largely unchanged. This guidance is effective for the fiscal years and interim periods within those years beginning after December 15, 2018, and requires a modified retrospective approach to adoption. The Company is currently evaluating the impact of adoption on its consolidated financial statements. The standard is expected to result in an increase in total assets and total liabilities, but will not have a significant impact on the consolidated statement of operations.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The core principle of the standard is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for the goods or services. In July 2015, the FASB postponed the effective date of this new guidance from January 1, 2017 to January 1, 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Company will adopt ASU No. 2014-09 on January 1, 2018 using the modified retrospective method of transition, which requires a cumulative-effect adjustment as of the date of adoption. The Company has concluded the adoption will not have a material impact on its consolidated financial statements. The adoption will result in additional disclosures associated with the disaggregation of revenue and performance obligations.

Note 3 — Compensation and Benefits

Compensation and benefits expenses to employees and members is comprised of the following:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Cash Compensation and Other Benefits	$48,722	$41,397	$35,431
Non-Cash Compensation	10,182	6,933	11,092
Total Compensation and Benefits Expense	$58,904	$48,330	$46,523

All non-cash compensation awards granted have varying vesting schedules and are issued at prices equal to the assessed fair market value at the time of issuance, as discussed below. Details of awards of Class B units of the operating company, Delayed Exchange Class B units, phantom Delayed Exchange Class B units, phantom Class B units of the operating company, options to purchase Class A common stock or Class B units, options to purchase Delayed Exchange Class B units, and shares of Class A common stock awarded for the three years ended December 31, 2017 are as follows:

	For the Years Ended December 31,					
	2017		2016		2015	
	Amount	Fair Value[1]	Amount	Fair Value[1]	Amount	Fair Value[1]
Restricted Class B Units	40,500	$11.11	5,812	$8.60	23,782	$9.46
Delayed Exchange Class B Units[2]	620,023	$7.11	—	$—	993,965	$5.21
Deferred Compensation Phantom Delayed Exchange Class B Units[3]	232,667	$7.04	367,214	$6.30	—	$—
Phantom Class B Units[4]	5,200	$9.61	—	$—	14,060	$7.11
Options to Purchase Shares of Class A Common Stock[5]	50,000	$3.04	—	$—	—	$—
Options to Purchase Class B Units[5]	320,000	$3.04	—	$—	—	$—
Options to Purchase Delayed Exchange Class B Units[6]	2,630,000	$2.30	—	$—	—	$—
Options to Purchase Shares of Class A Common Stock[7]	—	$—	—	$—	3,000,000	$1.18
Participating Shares of Class A Common Stock	—	$—	—	$—	31,010	$8.38
Restricted Shares of Class A Common Stock[8]	—	$—	—	$—	100,000	$6.08

1 Represents the weighted average grant date estimated fair value per share, unit, or option.

2 Represents Class B units issued under the 2006 Equity Incentive Plan (as defined below). These units vest immediately upon grant, but may not be exchanged pursuant to the Amended and Restated Operating Agreement of the operating company until the seventh anniversary of the date of grant. These units are also not entitled to any benefits under the Tax Receivable Agreement between the Company and members of the operating company. For the year-ended December 31, 2017, the Delayed Exchange Class B units were issued to certain employee members that elected to have their 2016 year-end cash compensation paid in the form of equity which were issued and vested immediately on January 1, 2017.

3 Represents phantom Delayed Exchange Class B units issued under the 2006 Equity Incentive Plan (as defined below). These phantom units vest ratably over four years, but may not be exchanged pursuant to the Amended and Restated Operating Agreement of the operating company until seven years after the date they vest. These units are also not entitled to any benefits under the Tax Receivable Agreement between the Company and members of the operating company.

4 Represents phantom Class B units issued under the 2006 Equity Incentive Plan (as defined below). These phantom units vest ratably over ten years and are not entitled to receive dividends or dividend equivalents until vested.

5 Represents options to purchase shares of Class A common stock or Class B units under the 2006 Equity Incentive Plan and 2007 Equity Incentive Plan (as defined below), respectively. These options become exercisable five years from the date of grant.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 3 — Compensation and Benefits (Continued)

6 Represents options to purchase Delayed Exchange Class B units issued under 2006 Equity Incentive Plan (as defined below). These options become exercisable five years from the date of grant. Upon exercise, the resulting Delayed Exchange Class B units may not be exchanged pursuant the Amended and Restated Operating Agreement until the seventh anniversary of the exercise date and are not entitled to any benefits under the Tax Receivable Agreement.

7 Represents options to purchase shares of Class A common stock issued whose vesting is contingent on meeting various performance goals. These options contingently vest over a period of seven years.

8 Represents restricted shares of Class A Common Stock that are not entitled to receive dividends or dividend equivalents until vested.

As part of the Company's year-end bonus structure, certain employee members may elect to have all or part of year-end cash compensation paid in the form of cash, or equity issued pursuant to Pzena Investment Management, LLC Amended and Restated 2006 Equity Incentive Plan ("the 2006 Equity Incentive Plan"). For the year ended December 31, 2017, $4.2 million of cash compensation was elected to be paid in the form of equity, which was issued and vested immediately on January 1, 2018. Details of these awards issued on January 1, 2018 are as follows:

	January 1, 2018	
	Amount	Fair Value[1]
Options to Purchase Delayed Exchange Class B Units[2]	1,062,820	$ 1.95
Delayed Exchange Class B Units[3]	300,931	$ 7.04

1 Represents the weighted average grant date estimated fair value per share, unit, or option as of December 31, 2017.

2 Represents options to purchase Delayed Exchange Class B units issued under 2006 Equity Incentive Plan. These options are exercisable on the date of grant. Upon exercise, the resulting Delayed Exchange Class B units may not be exchanged pursuant the Amended and Restated Operating Agreement until the seventh anniversary of the exercise date and are not entitled to any benefits under the Tax Receivable Agreement.

3 Represents Class B units issued under the 2006 Equity Incentive Plan. These units vest immediately upon grant, but may not be exchanged pursuant to the Amended and Restated Operating Agreement of the operating company until the seventh anniversary of the date of grant. These units are also not entitled to any benefits under the Tax Receivable Agreement between the Company and members of the operating company.

Pursuant to the 2006 Equity Incentive Plan, the operating company issues Class B units, phantom Class B units, and options to purchase Class B units. The Company also issues Delayed Exchange Class B units pursuant to the 2006 Equity Incentive Plan. These Delayed Exchange Class B units may not be exchanged pursuant to the Amended and Restated Operating Agreement of the operating company until at least the seventh anniversary of the date they vest. These Delayed Exchange Class B units are also not entitled to any benefit under the Tax Receivable Agreement between the Company and current, future and past members of the operating company. The Company also issues phantom Delayed Exchange Class B units and options to purchase Delayed Exchange Class B units. Under the Pzena Investment Management, Inc. 2007 Equity Incentive Plan ("the 2007 Equity Incentive Plan"), the Company issues shares of restricted Class A common stock, options to purchase Class A common stock and contingently vesting options to acquire shares of Class A common stock. During the year ended December 31, 2017, 1,000,000 contingently vesting options were forfeited in connection with an employee departure. Sadly, the Company's

Executive Vice President and Executive Committee member passed away on July 22, 2017. As a result, 549,888 phantom Class B units did not vest and were forfeited. During the year ended December 31, 2016 and 2015, 48,000 phantom Class B units and 5,775 restricted Class B units, respectively, were forfeited in connection with employee departures. During the years ended December 31, 2017, 2016 and 2015, no contingently vesting options vested. During the year ended December 31, 2015, 142,315 Delayed Exchange Class B units issued to one employee during 2014 were canceled. Additional compensation expense of less than $0.1 million was recognized upon cancellation and replacement of the award for cash. No Class B units were canceled during the years ended December 31, 2017 or 2016.

Under the Pzena Investment Management, LLC Amended and Restated Bonus Plan (the “Bonus Plan”), eligible employees whose compensation is in excess of certain thresholds are required to defer a portion of that excess. These deferred amounts may be invested, at the employee’s discretion, in certain investment options as designated by the Compensation Committee of the Company's Board of Directors. Amounts deferred in any calendar year reduce that year’s compensation expense and are amortized and vest ratably over a four year period commencing the following year. The Company also issued to certain of its employees deferred compensation with certain investment options that also vest ratably over a four years period. As of December 31, 2017 and 2016, the liability associated with deferred compensation investment accounts was $0.9 million and $4.2 million, respectively. During the year ended December 31, 2017, the vesting of 5,739 deferred compensation phantom Class B units and $1.5 million in deferred compensation investments was accelerated due to both the passing of the Company's

Executive Vice President and an employee departure. During the year ended December 31, 2016, approximately $0.2 million in deferred compensation investments were forfeited in connection with employee departures. There were no deferred compensation investment forfeitures under the Bonus Plan during the year ended December 31, 2015.

Pursuant to the Pzena Investment Management, Inc. Non-Employee Director Deferred Compensation Plan (the "Director Plan"), non-employee directors may elect to have all or part of the compensation otherwise payable in cash, deferred in the form of phantom shares of Class A common stock of the Company issued under the 2007 Equity Incentive Plan. Elections to defer compensation under the Director Plan are made on a year-to-year basis. Elections of deferred stock units result in the issuance of phantom shares of Class A common stock. Distributions under the Director Plan shall be made in a single distribution of shares of our Class A common stock at such time as elected by the participant when the deferral was made. Since inception of the Director Plan in 2009, the Company's directors have elected to defer 100% of their compensation in the form of phantom shares of Class A common stock. Amounts deferred in any calendar year are amortized over the calendar year and reflected as General and Administrative Expense. During the years ended December 31, 2017, 2016 and 2015, the directors were awarded 44,786, 58,645, and 42,196 phantom shares of Class A common stock, respectively, reflecting the annual deferral of compensation and additional phantom shares issued as of each date, and in the amount of dividends and/or special dividends and distributions that are paid with respect to Class A common stock of the Company. As of December 31, 2017 and 2016, there were 336,016 and 291,230 phantom shares of Class A common stock outstanding, respectively. There were no distributions made under the Director Plan during the years ended December 31, 2017 and 2016.

The Company uses a fair value method in recording the expense associated with the granting of Class B units, Delayed Exchange Class B units, phantom Class B units, options to purchase Class A common stock and Class B units, options to purchase Delayed Exchange Class B units, and shares of Class A common stock under the 2006 and 2007 Equity Incentive Plans, phantom Class B units and phantom Delayed Exchange Class B units under the Bonus Plan, and phantom shares of Class A common stock under the Director Plan.

The fair value of awarded restricted shares of Class A common stock under the 2007 Equity Incentive Plan and phantom shares of Class A common stock under the Director Plan is determined based on the closing market price of our Class A common stock on the date of grant. The fair value of awarded Class B units and phantom Class B units under the 2006 Equity Incentive Plan and phantom Class B units under the Bonus Plan is determined by reference to the market price of our Class A common stock on the date of grant, since Class B units are exchangeable for shares of our Class A common stock on a one-for-one basis and adjusted for the impact of award terms on the value of the award. Certain of the phantom Class B units and restricted shares of Class A common stock are not entitled to dividends or dividend equivalents while unvested. The fair value of these awards is determined based on the closing market price of our Class A common stock on the date of grant, net of the present value of the dividends using the applicable risk-free interest rate. The Delayed Exchange Class B Units have a seven years exchange limitation and are not entitled to any benefits under the tax receivable agreement. The fair value of these awards is determined based on the closing market price of our Class A common stock on the date of grant, net of the effects of the liquidity limitation and tax receivable agreement benefit exclusion. The Company also issued options to purchase Delayed Exchange Class B units. The fair value of these options is determined using an option pricing model where the strike price reflects the fair value of Delayed Exchange Class B units on the date of grant.

The fair value of options to purchase Class B units, shares of Class A common stock, and Delayed Exchange Class B units is determined by using an appropriate option pricing model on the grant date. No options were issued during the the year ended December 31, 2016. For each of the years ended December 31, 2017 and 2015 the Company issued options valued using the Black-Scholes option pricing model with the following weighted average assumptions:

	2017 January 1,	2015 March 2,	September 22,
Weighted Average Time Until Exercise	7 years	7 years	7 years
Expected Volatility	42 %	35 %	40 %
Risk-Free Rate	2.25 %	1.89 %	1.83 %
Dividend Yield	3.15 %	4.83 %	5.02 %

Weighted Average Time Until Exercise — The expected term is based on the Company’s historical experience and the particular terms of its option awards.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 3 — Compensation and Benefits (Continued)

Expected Volatility — Due to the lack of sufficient historical data for the Company's own shares, the Company based its expected volatility on a representative peer group.

Risk-Free Rate — The risk-free rate for periods within the expected term of the options is based on the interest rate of a traded zero-coupon U.S. Treasury bond with a term equal to the options' expected term on the date of grant.

Dividend Yield — The dividend yield is based on the Company's anticipated dividend payout over the expected term of the option awards.

The following is a summary of the option activity for the three years ended December 31, 2017:

	For the Years Ended December 31,					
	2017		2016		2015	
	Options Outstanding	Weighted Average Exercise Price	Options Outstanding	Weighted Average Exercise Price	Options Outstanding	Weighted Average Exercise Price
Beginning Balance	4,703,722	$ 11.53	5,156,143	$ 11.01	3,114,282	$ 7.10
Options Granted[1]	3,000,000	7.95	—	—	3,000,000	13.00
Options Cancelled	(1,163,310)	13.07	(9,044)	7.93	—	—
Options Exercised	(348,910)	9.98	(443,377)	5.56	(958,139)	4.52
Ending Balance	6,191,502	$ 9.59	4,703,722	$ 11.53	5,156,143	$ 11.01

1 Options granted for the year-ended December 31, 2017 include 2,630,000 of options to purchase Delayed Exchange Class B units, 320,000 options to purchase Class B units, and 50,000 options to purchase Class A common stock.

The weighted average grant-date fair values per options issued in 2017 and 2015 were $2.39 and $1.18, respectively. No options were issued in 2016. The 348,910 options exercised in 2017 resulted in 41,781 net Class B units issued, as a result of the redemption of 257,129 Class B units for the cashless exercise of the options and 16,722 net Class A shares issued, as a result of the redemption of 33,278 Class A shares for the cashless exercise of options. The 443,377 options exercised in 2016 resulted in 282,519 net Class B units issued, as a result of the redemption of 160,858 Class B units for the cashless exercise of the options and $0.9 million in cash. The 958,139 options to purchase Class B units that were exercised in 2015 resulted in 715,706 net Class B units issued, as a result of the redemption of 239,058 Class B units for the cashless exercise of the options and $1.7 million in cash and 962 shares of Class A common stock, as a result of the redemption of 2,413 shares of Class A common stock for the cashless exercise of the options. The 1,163,310 and 9,044 options to purchase Class B units that were cancelled during 2017 and 2016, respectively, were in connection with employee departures and option expirations.

Exercise prices for options outstanding and exercisable as of December 31, 2017 are as follows:

	Options Outstanding			Options Exercisable		
	Number Outstanding as of December 31, 2017	Weighted-Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable as of December 31, 2017	Weighted-Average Remaining Contractual Life	Weighted Average Exercise Price
$4.22 – $5.00	131,334	2.4	$ 4.48	131,334	2.4	$ 4.48
$5.00 – $10.00	3,502,646	7.3	7.32	872,646	2.1	7.94
$10.00 – $15.00	2,557,522	5.0	12.98	187,522	2.4	10.93

$4.22 – $15.00	6,191,502	6.2	$ 9.59	1,191,502	2.2	$ 8.03

Based on the closing market price of the Company's Class A common stock on December 31, 2017, the aggregate intrinsic value of the Company's options was as follows:

	Options Outstanding	Options Exercisable
	(in thousands)	
Aggregate Intrinsic Value	$12,593	$ 3,230

F-20

TABLE OF CONTENTS
Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 3 — Compensation and Benefits (Continued)

Phantom Class B units and Phantom Delayed Exchange Class B units issued pursuant to the Bonus Plan, which vest ratably over four years, are summarized as follows:

	For the Years Ended December 31,					
	2017		2016		2015	
	Phantom Units Outstanding	Weighted Average Price	Phantom Units Outstanding	Weighted Average Price	Phantom Units Outstanding	Weighted Average Price
Beginning Balance	335,569	$ 6.52	28,607	$ 7.95	71,688	$ 6.63
Phantom Delayed Exchange Class B Units Issued[1]	232,667	7.04	367,214	6.30	—	—
Vesting of Phantom Delayed Exchange Class B Units[1]	(91,805)	6.30	(37,384)	5.12	—	—
Vesting of Phantom Class B Units	(5,739)	11.76	(22,868)	7.00	(43,081)	5.75
Ending Balance	470,692	$ 6.76	335,569	$ 6.52	28,607	$ 7.95

1 Represents phantom Delayed Exchange Class B units issued under the 2006 Equity Incentive Plan. These phantom units vest ratably over four years, but may not be exchanged pursuant to the Amended and Restated Operating Agreement of the operating company until seven years after the date they vest. These units are also not entitled to any benefits under the Tax Receivable Agreement between the Company and members of the operating company.

Phantom Class B units issued pursuant to the 2006 Equity Incentive Plan, which vest ratably over 10 years and are not eligible to receive dividends or dividend equivalents until vested, are summarized as follows:

	For the Years Ended December 31,					
	2017		2016		2015	
	Phantom Units Outstanding	Weighted Average Price	Phantom Units Outstanding	Weighted Average Price	Phantom Units Outstanding	Weighted Average Price
Beginning Balance	2,599,656	$ 4.92	3,066,325	$ 4.94	3,476,934	$ 4.92
Phantom Class B Units Issued	5,200	9.61	—	—	14,060	7.11
Vesting of Phantom Class B Units	(329,503)	4.89	(418,669)	4.79	(424,669)	4.83
Phantom Class B Units Forfeited	(549,888)	4.55	(48,000)	7.62	—	—
Ending Balance	1,725,465	$ 5.05	2,599,656	$ 4.92	3,066,325	$ 4.94

As of December 31, 2017 and 2016, the Company had approximately $32.6 million and $30.0 million, respectively, in unrecorded compensation expense related to unvested awards issued pursuant to its Bonus Plan; Class B units, option grants, and phantom Class B units issued under the 2006 Equity Incentive Plan; and restricted Class A common stock issued under the 2007 Equity Incentive Plan. The Company anticipates that this unrecorded cost will amortize over the respective vesting periods of the awards.

As of December 31, 2017, the total units and shares remaining available for future issuance under the equity incentive plans are as follows:

Plan	Number of Securities Remaining Available For Future Issuance

	Under Equity Incentive Plans
Pzena Investment Management, LLC 2006 Equity Incentive Plan	15,254,833
Pzena Investment Management, Inc. 2007 Equity Incentive Plan	13,306,893
Total	28,561,726

F-21

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 4 — Employee Benefit Plans

The Profit Sharing and Savings Plan is a defined contribution profit sharing plan with a 401(k) deferral component. All full-time employees and certain part-time employees who have met the age and length of service requirements are eligible to participate in the plan. The plan allows participating employees to make elective deferrals of compensation up to the annual limits which are set by law. The plan provides for a discretionary annual contribution by the operating company which is determined by a formula based on the salaries of eligible employees as defined by the plan. During the years ended December 31, 2017, 2016, and 2015, the expense recognized in connection with this plan was $0.9 million, $0.8 million, and $0.8 million, respectively.

Note 5 — Earnings per Share

Basic earnings per share is computed by dividing the Company's net income attributable to its common stockholders by the weighted average number of shares outstanding during the reporting period.

Under the two-class method of computing basic earnings per share, basic earnings per share is calculated by dividing net income for basic earnings per share by the weighted average number of common shares outstanding during the period. The two-class method includes an earnings allocation formula that determines earnings per share for each participating security according to dividends declared and undistributed earnings for the period. The Company's net income for basis earnings per share is reduced by the amount allocated to participating restricted shares of Class A common stock which participate for purposes of calculating earnings per share.

For the years ended December 31, 2017, 2016, and 2015, the Company's basic earnings per share was determined as follows:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands, except share and per share amounts)		
Net Income Allocated to:			
Class A Common Stock	$6,907	$ 16,164	$ 7,665
Participating Shares of Restricted Class A Common Stock	1	15	14
Net Income for Basic Earnings Per Share	$6,908	$ 16,179	$ 7,679
Basic Weighted-Average Shares Outstanding	17,335,689	15,945,275	13,989,589
Add: Participating Shares of Restricted Class A Common Stock[1]	2,659	17,627	24,630
Total Basic Weighted-Average Shares Outstanding	17,338,348	15,962,902	14,014,219
Basic Earnings per Share	$0.40	$ 1.01	$ 0.55

1 Certain unvested shares of Class A common stock granted to employees have nonforfeitable rights to dividends and therefore participate fully in the results of the Company from the date they are granted. They are included in the computation of basic earnings per share using the two-class method for participating securities.

Diluted earnings per share adjusts this calculation to reflect the impact of all outstanding membership units of the operating company, phantom Class B units, phantom Class A common stock, outstanding Class B unit options, options to purchase Class A common stock, and restricted Class A common stock, to the extent they would have a dilutive effect on earnings per share for the reporting period. Net income for diluted earnings per share generally assumes all outstanding operating company membership units are converted into Company stock at the beginning of the reporting period and the resulting change to the Company's net income associated with its increased interest in the operating company is taxed at the Company's effective tax rate, exclusive of one-time charges and adjustments associated with both the valuation allowance and the liability to selling and converting shareholders. When this conversion results in an increase in earnings per share or a decrease in loss per share, diluted net income and diluted earnings per share are assumed to be equal to basic net income and basic earnings per share for the reporting period.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 5 — Earnings per Share (Continued)

For the years ended December 31, 2017, 2016, and 2015, the Company's diluted net income was determined as follows:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Net Income Attributable to Non-Controlling Interests of Pzena Investment Management, LLC	$52,379	$37,065	$41,562
Less: Assumed Corporate Income Taxes	19,223	13,644	15,432
Assumed After-Tax Income of Pzena Investment Management, LLC	33,156	23,421	26,130
Net Income of Pzena Investment Management, Inc	6,908	16,179	7,679
Diluted Net Income	$40,064	$39,600	$33,809

Under the two-class method, earnings per share is calculated by dividing net income for diluted earnings per share by the weighted average number of common shares outstanding during the period, plus the dilutive effect of any potential common shares outstanding during the period using the more dilutive of the treasury method or two-class method. The two-class method includes an earnings allocation formula that determines earnings per share for each participating security according to dividends declared and undistributed earnings for the period. The Company's net income for diluted earnings per share is reduced by the amount allocated to participating Class B units for purposes of calculating earnings per share. Dividends paid per share on the unvested Class B units are equal to the dividends paid per share of Class A common stock of the Company.

For the years ended December 31, 2017, 2016, and 2015, the Company's diluted earnings per share were determined as follows:

	For the Years Ended December 31,		
	2017	2016	2015
	(In thousands, except share and per share amounts)		
Diluted Net Income Allocated to:			
Class A Common Stock	$40,025	$ 39,561	33,751
Participating Shares of Restricted Class A Common Stock	1	15	14
Participating Class B Units	38	24	44
Total Diluted Net Income Attributable to Shareholders	$40,064	$ 39,600	$ 33,809
Basic Weighted-Average Shares Outstanding	17,338,348	15,962,902	14,014,219
Dilutive Effect of Class B Units	51,108,030	51,289,167	52,072,070
Dilutive Effect of Options[1]	583,669	326,145	555,940
Dilutive Effect of Phantom Units	1,767,130	1,189,273	1,349,050
Dilutive Effect of Restricted Shares of Class A Common Stock[2]	72,299	40,628	51,760
Dilutive Weighted-Average Shares Outstanding	70,869,476	68,808,115	68,043,039
Add: Participating Class B Units[3]	64,886	41,057	83,747
Total Dilutive Weighted-Average Shares Outstanding	70,934,362	68,849,172	68,126,786
Diluted Earnings per Share[4]	$0.56	$ 0.58	$ 0.50

1 Represents the dilutive effect of options to purchase Class B units and Class A common stock.

2 Certain restricted shares of Class A common stock granted to employees are not entitled to dividend or dividend equivalent payments until they are vested and are therefore non-participating securities and are not included in the computation of basic earnings per share. They are included in the computation of diluted earnings per share when the effect is dilutive using the treasury stock method.

3 Unvested Class B Units granted to employees have nonforfeitable rights to dividends and therefore participate fully in the results of the operating company's operations from the date they are granted. They are included in the computation of diluted earnings per share using the two-class method for participating securities.

4 Reflects the calculation of diluted earnings per share which results in an increase in earnings per share during the year ended December 31, 2017. Therefore, diluted earnings per share is presented on the statement of operations equal to basic earnings per share.

Approximately 0.6 million options to purchase Class B units, 0.1 million options to purchase shares of Class A common stock, and 2.0 million contingent options to purchase shares of Class A common stock were excluded from the calculation of diluted earnings per share for the year ended December 31, 2017, as their inclusion would have had an antidilutive effect based on current market prices or because the option had contingent vesting requirements that were not met. Approximately 0.6 million options to purchase Class B units and 3.0 million contingent options to purchase Class A common stock were excluded from the calculation of diluted earnings per share for both the years ended December 31, 2016 and 2015, as their inclusion would have had an antidilutive effect based on current market prices or because the option had contingent vesting requirements that were not met.

Note 6 — Shareholders' Equity

The Company functions as the sole managing member of the operating company. As a result, the Company: (i) consolidates the financial results of the operating company and reflects the membership interest in it that it does not own as a non-controlling interest in its consolidated financial statements; and (ii) recognizes income generated from its economic interest in the operating company's net income. Class A and Class B units of the operating company have the same economic rights per unit. As of December 31, 2017, the holders of Class A common stock (through the Company) and the holders of Class B units of the operating company held approximately 26.3% and 73.7%, respectively, of the economic interests in the operations of the business. As of December 31, 2016, the holders of Class A common stock (through the Company) and the holders of Class B units of the operating company held approximately 25.6% and 74.4%, respectively, of the economic interests in the operations of the business.

Each Class B unit of the operating company has a corresponding share of the Company's Class B common stock, par value $0.000001 per share. Each share of the Company's Class B common stock entitles its holder to five votes, until the first time that the number of shares of Class B common stock outstanding constitutes less than 20% of the number of all shares of the Company's common stock outstanding. From this time and thereafter, each share of the Company's Class B common stock entitles its holder to one vote. When a Class B unit is exchanged for a share of the Company's Class A common stock or forfeited, a corresponding share of the Company's Class B common stock will automatically be redeemed and canceled. Conversely, to the extent that the Company causes the operating company to issue additional Class B units to employees pursuant to its equity incentive plan, these additional holders of Class B units would be entitled to receive a corresponding number of shares of the Company's Class B common stock (including if the Class B units awarded are subject to vesting).

All holders of the Company's Class B common stock have entered into a stockholders' agreement, pursuant to which they agreed to vote all shares of Class B common stock then held by them, with the majority of votes of Class B common stockholders taken in a preliminary vote of the Class B common stockholders.

The outstanding shares of the Company's Class A common stock represent 100% of the rights of the holders of all classes of the Company's capital stock to receive distributions, except that holders of Class B common stock will have the right to receive the class's par value upon the Company's liquidation, dissolution or winding up.

Pursuant to the operating agreement of the operating company, each vested Class B unit is exchangeable for a share of the Company's Class A common stock, subject to certain exchange timing and volume limitations.

On December 21, 2017, December 22, 2016, May 12, 2016, and July 27, 2015 certain of the operating company's members exchanged an aggregate of 855,535, 1,056,929, 1,369,811, and 2,772,171, respectively, of their Class B units for an equivalent number of shares of Class A common stock of the Company. These acquisitions of additional operating company membership interests were treated as reorganizations of entities under common control as required by the Business Combinations Topic of the FASB ASC.

TABLE OF CONTENTS

Pzena Investment Management, Inc.

Notes to Consolidated Financial Statements (Continued)

Note 6 — Shareholders' Equity (Continued)

The incremental assets and liabilities assumed in the exchanges were recorded on December 21, 2017, December 22, 2016, May 12, 2016, and July 27, 2015 as follows:

	December 21, 2017	December 22, 2016	May 12, 2016	July 27, 2015
	(in thousands)			
Pzena Investment Management, LLC Members' Capital	$11,453	$ 14,282	$18,545	$37,760
Pzena Investment Management, LLC Accumulated Deficit	(10,396)	(13,299)	(17,475)	(35,482)
Realizable Deferred Tax Asset	2,090	1,130	1,244	3,301
Net Tax Receivable Liability to Converting Unitholders	(1,538)	(961)	(1,058)	(2,806)
Total	$1,609	$ 1,152	$1,256	$2,773
Common Stock, at Par	$9	$ 10	$13	$28
Additional Paid-in Capital	1,600	1,142	1,243	2,745
Total	$1,609	$ 1,152	$1,256	$2,773

The Company announced a share repurchase program on April 24, 2012. The Board of Directors authorized the Company to repurchase an aggregate of $10 million of the Company’s outstanding Class A common stock and the operating company’s Class B units on the open market and in private transactions in accordance with applicable securities laws. On February 5, 2014, the Board of Directors authorized the Company to repurchase an additional $20 million of the Company's outstanding Class A common stock and Class B units of the operating company. The timing, number and value of common shares and units repurchased are subject to the Company’s discretion. The Company’s share repurchase program is not subject to an expiration date and may be suspended, discontinued, or modified at any time, for any reason.

During the year ended December 31, 2017, the Company purchased and retired 150,727 shares of Class A common stock and 33,715 Class B units at an average price per share of $9.88 and $10.89, respectively. During the year ended December 31, 2016, the Company purchased and retired 339,939 shares of Class A common stock and 72,860 Class B units at an average price per share of $7.88 and $10.72, respectively. During the year ended December 31, 2015, the Company purchased and retired 629,174 shares of Class A common stock and 192,406 Class B units at an average price per share of $9.18 and $10.52, respectively. The Company records the repurchase of shares and units at cost based on the trade date of the transaction.

During the years ended December 31, 2017, 2016, and 2015, 31,803, 87,563 and 78,093 Delayed Exchange Class B units were issued for approximately $0.2 million, $0.4 million, and $0.4 million in cash, respectively, to certain employee members pursuant to the 2006 Equity Incentive Plan.

Note 7 — Non-Controlling Interests

Non-Controlling Interests in the operations of the Company’s operating company and consolidated subsidiaries are comprised of the following:

	For the Years Ended December 31,		
	2017	2016	2015
	(in thousands)		
Non-Controlling Interests of Pzena Investment Management, LLC	$52,379	$37,065	$41,562
Non-Controlling Interests of Consolidated Subsidiaries	863	407	(2,238)

Non-Controlling Interests	$53,242	$37,472	$39,324

Distributions to non-controlling interests represent tax allocations and dividend equivalents paid to the members of the operating company, as well as redemptions by investors in the Company’s consolidated subsidiaries.

TABLE OF CONTENTS

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 8 — Investments

The following is a summary of Investments:

	As of December 31, 2017	December 31, 2016
	(in thousands)	
Investment securities, trading		
Equity Securities	$5,452	$ 14,323
Total investment securities, trading	$5,452	$ 14,323
Investments in equity method investees	16,285	7,987
Total	$21,737	$ 22,310

Investment Securities, Trading

Investments, at Fair Value consisted of the following at December 31, 2017:

	Cost	Unrealized Gain/(Loss)	Fair Value
	(in thousands)		
Equity Securities	$4,399	$ 1,053	$5,452
Total	$4,399	$ 1,053	$5,452

Investments, at Fair Value consisted of the following at December 31, 2016:

	Cost	Unrealized Gain/(Loss)	Fair Value
	(in thousands)		
Equity Securities	$13,105	$ 1,218	$14,323
Total	$13,105	$ 1,218	$14,323

Securities Sold Short, at Fair Value consisted of the following at December 31, 2016:

	Cost	Unrealized (Gain)/Loss	Fair Value
	(in thousands)		
Securities Sold Short	$2,646	$ (24)	$2,622
Total	$2,646	$ (24)	$2,622

Investments in Equity Method Investees

The operating company sponsors and provides investment management services to certain private investment partnerships and Pzena mutual funds through which it offers its investment strategies. The Company has made investments in certain of these private investment partnerships and mutual funds to satisfy its obligations under the Company's deferred compensation program and provide the initial cash investment in our mutual funds. The Company holds a non-controlling interest and exercises significant influence in these entities, and accounts for its investments as equity method investments which are included in Equity Method Investments on the consolidated statements of financial condition. On November 9, 2017 and December 21, 2017 due to additional subscriptions into the Pzena Mid Cap Value Fund and Pzena Long/Short Value Fund, respectively, the Company's ownership decreased to 41.7% and 35.5%, respectively. As the Company was no longer deemed to control the funds, it deconsolidated the entities, removed the related assets, liabilities and non-controlling interest from its balance sheet and classified the Company's remaining investments as an equity method investments. As of December 31, 2017, the Company's investments range between 1% and 36% of the capital of these entities and have an aggregate carrying value of $16.3 million.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 9 — Fair Value Measurements

The Fair Value Measurements and Disclosures Topic of the FASB ASC defines fair value as the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date. The Fair Value Measurements and Disclosures Topic of the FASB ASC also establishes a framework for measuring fair value and a valuation hierarchy based upon the transparency of inputs used in the valuation of an asset or liability. Classification within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The valuation hierarchy contains three levels: (i) valuation inputs are unadjusted quoted market prices for identical assets or liabilities in active markets (Level 1); (ii) valuation inputs are quoted prices for identical assets or liabilities in markets that are not active, quoted market prices for similar assets and liabilities in active markets, and other observable inputs directly or indirectly related to the asset or liability being measured (Level 2); and (iii) valuation inputs are unobservable and significant to the fair value measurement (Level 3).

Included in the Company's consolidated statements of financial condition are investments in equity securities and securities sold short, both of which are exchange-traded securities with quoted prices in active markets. The fair value measurements of the equity securities, securities sold short, have been classified as Level 1. The investments in equity method investees are held at their carrying value.

The following tables present these instruments' fair value at December 31, 2017:

	Level 1	Level 2	Level 3	Total
	(in thousands)			
Assets:				
Equity Securities	$5,452	$ —	$ —	$5,452

The following tables present these instruments' fair value at December 31, 2016:

	Level 1	Level 2	Level 3	Total
	(in thousands)			
Assets:				
Equity Securities	$14,323	$ —	$ —	$14,323

	Level 1	Level 2	Level 3	Total
	(in thousands)			
Liabilities:				
Securities Sold Short	$2,622	$ —	$ —	$2,622

Transfers among levels, if any, are recorded as of the beginning of the reporting period. For the years ended December 31, 2017, and 2016, there were no transfers between levels. In addition, the Company did not hold any Level 2 or Level 3 securities during these periods.

F-27

TABLE OF CONTENTS

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 10 — Property and Equipment

Property and equipment, net, is comprised of the following:

	As of December 31, 2017	December 31, 2016
	(in thousands)	
Leasehold Improvements	$6,832	$ 6,832
Furniture and Fixtures	1,190	1,190
Computer Hardware	686	756
Computer Software	333	238
Office Equipment	281	209
Total	9,322	9,225
Less: Accumulated Depreciation and Amortization	(3,063)	(2,260)
Total	$6,259	$ 6,965

During the year ended December 31, 2015, the Company moved to its new corporate headquarters, as discussed further in Note 12—Commitments and Contingencies, and began depreciating approximately $6.8 million in leasehold improvements and $1.2 million in furniture and fixtures related to this new office space. The Company recognized a $0.4 million loss on the disposal of fixed assets associated with the retirement of assets in our former corporate headquarters, which is included in general and administrative expense. No such losses were recognized during the years ended December 31, 2017 and 2016.

Depreciation is included in general and administrative expense and totaled $1.0 million, $1.1 million, and $0.8 million for each of the years ended December 31, 2017, 2016, and 2015, respectively.

Note 11 — Related Party Transactions

For the years ended December 31, 2017, 2016, and 2015, the Company earned $0.4 million, $0.3 million, and $3.2 million, respectively, in investment advisory fees from unconsolidated VIEs which receive investment management services from the Company.

During the year ended December 31, 2017 and 2016, the Company offered loans to employees, excluding executive officers, for the purpose of financing tax obligations associated with compensatory stock and unit vesting. Loans are generally written for a seven-year period, at an interest rate equivalent to the Applicable Federal Rate, payable in annual installments, and collateralized by units held by the employee. These loans are full recourse in nature and totaled $1.4 million and $0.9 million at December 31, 2017 and 2016, respectively.

The operating company, as the investment adviser for certain Pzena branded SEC-registered mutual funds, private placement funds, and non-U.S. funds, has contractually agreed to waive a portion or all of its management fees and pay fund expenses to ensure that the annual operating expenses of the funds stay below certain established total expense ratio thresholds. The Company recognized $1.1 million of such expenses for the year ended December 31, 2017, and $1.1 million for both the years ended December 31, 2016 and 2015.

The operating company manages the personal funds of certain of the Company's employees, including the CEO and its two Presidents. The operating company also manages accounts beneficially owned by a private fund in which certain of the Company's executive officers invest. Investments by employees in individual accounts are permitted only at the discretion of the executive committee of the operating company, but are generally not subject to the same minimum investment levels that are required of outside investors. The operating company also manages the personal funds of some of its employees' family members. Pursuant to the respective investment management agreements, the operating company waives or reduces its regular advisory fees for these accounts and personal funds. In addition, the operating company pays custody and administrative fees for certain of these accounts and personal funds in order to incubate products or preserve performance history. The aggregate value of the fees that the Company waived related to the Company's executive officers, other employees, and family members, was approximately $0.8 million for the year ended December 31, 2017, and $0.7 million in both of the years ended December

31, 2016 and 2015. The aggregate value of the custody and administrative fees paid related to the Company's executive offers, other employees, and family members was approximately $0.1 million in each of the years 2017, 2016, and 2015.

Pursuant to a tax receivable agreement signed between the members of the operating company and the Company, 85% of the cash savings generated by tax elections discussed in Note 13 — Income Taxes, are distributed to the selling and converting shareholders upon the realization of this benefit. For the years ended December 31, 2017 and 2016, $1.0 million and $0.8 million, respectively, of such payments were made to certain directors, executive officers and employees of the Company.

Note 12 — Commitments and Contingencies

In the normal course of business, the Company enters into agreements that include indemnities in favor of third parties, such as engagement letters with advisers and consultants. In certain cases, the Company may have recourse against third parties with respect to these indemnities. The Company maintains insurance policies that may provide coverage against certain claims under these indemnities. The Company has had no claims or payments pursuant to these agreements, and it believes the likelihood of a claim being made is remote. Utilizing the methodology in the Guarantees Topic of the FASB ASC, the Company's estimate of the value of such guarantees is de minimis, and, therefore, no accrual has been made in the consolidated financial statements.

During the year ended December 31, 2015, the Company moved to its new corporate headquarters. The new office space is leased under a non-cancellable operating lease agreement that expires on December 31, 2025. The Company reflects minimum lease expense for its headquarters on a straight-line basis over the lease term. During September 2016, the Company terminated its five-year sublease agreement which commenced on May 1, 2015. The Company entered into a new four-year sublease agreement commencing on October 1, 2016 that is cancellable by either the Company or sublessee given appropriate notice after the thirty-first month following the commencement of the sublease agreement. Sublease income will continue to decrease annual lease expense by approximately $0.4 million per year.

The Company's former headquarters were leased under a non-cancellable operating lease agreement which expired on October 31, 2015. The Company reflected minimum lease expense for its headquarters on a straight-line basis over the lease term. During the year ended December 31, 2011, the Company entered into a non-cancellable sublease agreement for certain excess office space associated with its operating lease agreement. The sublease agreement also expired on October 31, 2015. During the year ended December 31, 2015, $1.0 million in losses for the remaining rent and expected disposal costs and $0.4 million of non-recurring rent expense associated with exiting the former headquarters were recognized in general and administrative expense.

Lease expenses, including the losses and expenses recorded during 2015 which we do not expect to recur, were $2.1 million, $1.9 million, and $3.2 million, respectively, for the years ended December 31, 2017, 2016, and 2015 and are included in general and administrative expense. Lease expense for each of the years ended December 31, 2017 and 2016, was net of $0.4 million in sublease income. Future minimum lease payments are as follows:

Year Ending December 31,	Minimum Payments[1]
	(in thousands)
2018	1,979

2019	1,979
2020	1,979
2021	1,979
2022	1,979
2023 and thereafter	5,938
Total	$ 15,833

(1) Amounts have not been reduced by future minimum sublease payments of $0.8 million due under the two years, seven months non-cancellable sublease agreement.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 13 — Income Taxes

The operating company is a limited liability company that has elected to be treated as a partnership for tax purposes. Neither it nor the Company's other consolidated subsidiaries have made a provision for federal or state income taxes because it is the individual responsibility of each of these entities' members (including the Company) to separately report their proportionate share of the respective entity's taxable income or loss. The operating company has made a provision for New York City UBT and its U.K. consolidated subsidiary has made a provision for U.K. corporate taxes. The Company, as a "C" corporation under the Internal Revenue Code, is liable for federal, state and local taxes on the income derived from its economic interest in its operating company, which is net of UBT and U.K. taxes. Correspondingly, in its consolidated financial statements, the Company reports both the operating company's provision for UBT and U.K. taxes, as well as its provision for federal, state and local corporate taxes. The components of the income tax expense/ (benefit) are as follows:

	For the Year Ended December 31,		
	2017	2016[1]	2015
	(in thousands)		
Current Provision:			
Unincorporated and Other Business Taxes	$2,846	$1,583	$2,204
Local Corporate Tax	—	—	—
State Corporate Tax	—	—	—
Federal Corporate Tax	5	—	—
Total Current Provision	$2,851	$1,583	$2,204
Deferred Provision:			
Unincorporated and Other Business Taxes	$16	$5	$24
Local Corporate Tax	423	258	321
State Corporate Tax	263	199	200
Federal Corporate Tax	5,497	3,478	3,639
Total Deferred Provision	$6,199	$3,940	$4,184
Impact of Tax Cuts and Jobs Act[2]	26,468	—	—
Impact of Change in Historical 754 Step-Up Calculations[3]	(1,006)	—	—
Change in Valuation Allowance	—	(61,942)	(1,274)
Net Adjustment to Deferred Tax Asset[4]	—	1,944	—
Total Income Tax Expense/ (Benefit)	$34,512	$(54,475)	$5,114

1 During the year ended December 31, 2016, the operating company recognized a $0.7 million tax benefit associated with the reversal of uncertain tax position liabilities and interest related to unincorporated and other business tax expenses.

2 Reflects income tax expense resulting from the re-measurement of the deferred tax asset related to the Tax Cuts and Jobs Act enacted in the United States during the fourth quarter of 2017.

3 Reflects the net impact of a change in the historical calculation of the 754 step-ups and related deferred tax asset and corresponding liability to selling and converting shareholders recognized during the year-ended December 31, 2017.

4 During 2016, the Company recognized the net impact of the changes in the deferred tax asset and valuation allowance assessed against the deferred tax asset associated with the changes in expected future tax benefits.

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 13 — Income Taxes (Continued)

A reconciliation between the provision for income taxes reported for financial reporting purposes, and the application of the statutory U.S. Federal tax rate to the reported income before income taxes for the years ended December 31, 2017, 2016, and 2015, were as follows:

	For the Year Ended December 31,					
	2017		2016[1]		2015[1]	
	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income
	(in thousands, except % amounts)					
Federal Corporate Tax	$32,185	34.0 %	$(280)	34.0 %	$17,720	34.0 %
State and Local Corporate Tax, net of Federal Benefit	686	0.7 %	457	(55.5)%	1,631	3.1 %
Unincorporated and Other Business Tax[2]	1,889	2.0 %	1,048	(127.2)%	1,401	2.7 %
Non-Controlling Interests	(18,102)	(19.1)%	(12,740)	1,546.2 %	(14,601)	(28.0)%
Increase/(Decrease) in Liability to Selling and Converting Shareholders	(7,078)	(7.5)%	17,490	(2,122.6)%	144	0.3 %
Impact of Tax Cuts and Jobs Act[3]	26,468	28.0 %	—	— %	—	— %
Impact of Change in Historical 754 Step-Up Calculations[4]	(1,006)	(1.1)%	—	— %	—	— %
Deferred Income Tax Valuation Allowance	—	— %	(61,942)	7,517.2 %	(1,274)	(2.5)%
Net Adjustment to Deferred Tax Asset[5]	—	— %	1,944	(235.9)%	—	— %
Other	(530)	(0.5)%	(452)	54.8 %	93	0.2 %
Income Tax Expense	$34,512	36.5 %	$(54,475)	6,611.0 %	$5,114	9.8 %

1 The impact related to the use of net operating losses as presented in the 2016 and 2015 consolidated notes to financial statements have been reclassified to be included with Other tax rate items.

2 During the year ended December 31, 2016, the operating company recognized a $0.7 million tax benefit associated with the reversal of uncertain tax position liabilities and interest related to unincorporated and other business tax expenses.

3 Reflects income tax expense resulting from the re-measurement of the deferred tax asset related to the Tax Cuts and Jobs Act enacted in the United States during the fourth quarter of 2017.

4 Reflects the net impact of a change in the calculation of historical 754 step-ups and related deferred tax assets and corresponding liability to selling and converting shareholders recognized during the year-ended December 31, 2017.

5 During 2016, the Company recognized adjustments to the deferred tax asset and valuation allowance assessed against the deferred tax asset associated with a change in the effective tax rate.

The Income Taxes Topic of the FASB ASC establishes the minimum threshold for recognizing, and a system for measuring, the benefits of tax return positions in financial statements.

A reconciliation of the beginning and ending amount of total unrecognized tax benefits for the years ended December 31, 2017 and 2016 are as follows:

	For the Year Ended December 31, 2017 (in thousands)
Balance at December 31, 2016	$ 2,802

Increases Related to Current Year Tax Positions	1,870
Balance at December 31, 2017	$ 4,672

F-31

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 13 — Income Taxes (Continued)

	For the Year Ended December 31, 2016 (in thousands)
Balance at December 31, 2015	$ 2,318
Decreases Related to Prior Year Tax Positions	(664)
Increases Related to Current Year Tax Positions	1,210
Decreases Related to Settlements with Taxing Authorities	(62)
Balance at December 31, 2016	$ 2,802

The Company recognizes accrued interest and penalties related to unrecognized tax benefits as a component of Income Tax Expense/ (Benefit) on the consolidated statements of operations. As of December 31, 2017 and 2016, the Company had $4.7 million and $2.8 million in unrecognized tax benefits, that, if recognized, would affect the provision for income taxes. As of December 31, 2017 and 2016, the Company had interest related to unrecognized tax benefits of $0.5 million and $0.3 million, respectively. As a result of legislative changes, changes in judgment related to recognition or measurement, or potential settlements with taxing authorities, it is reasonably possible that the company's gross unrecognized tax benefits balance may change within the next twelve months by a range of zero to $3.4 million.

The Company and the operating company are generally no longer subject to U.S. Federal or state and local income tax examinations by tax authorities for any year prior to 2014. All tax years subsequent to, and including, 2014 are considered open and subject to examination by tax authorities.

As of both December 31, 2017 and 2016, the Company had available for U.S. Federal, state and local income tax reporting purposes, a net operating loss carryforward of $5.3 million and $10.2 million, respectively, which expires in varying amounts during the tax years 2029 through 2035.

The acquisition of the Class B units of the operating company, noted below, has allowed the Company to make an election under Section 754 of the Internal Revenue Code (“Section 754”) to step up its tax basis in the net assets acquired. This step up is deductible for tax purposes over a 15-year period.

Pursuant to a tax receivable agreement signed between the members of the operating company and the Company, 85% of the cash savings generated by this election will be distributed to the selling and converting shareholders upon the realization of this benefit.

If the Company exercises its right to terminate the tax receivable agreement early, the Company will be obligated to make an early termination payment to the selling and converting shareholders, based upon the net present value (based upon certain assumptions and deemed events set forth in the tax receivable agreement) of all payments that would be required to be paid by the Company under the tax receivable agreement. If certain change of control events were to occur, the Company would be obligated to make an early termination payment.

As discussed in Note 6, Shareholders’ Equity, on December 21, 2017, December 22, 2016, May 12, 2016, and July 27, 2015, certain of the operating company’s members exchanged an aggregate of 855,535, 1,056,929, 1,369,811, and

2,772,171,
respectively, of their Class B units for an equivalent number of shares of Class A common stock of the Company. The Company elected to step up its tax basis in the incremental assets acquired in accordance with Section 754. Based on the exchange-date fair values of the Company's common stock and the tax basis of the operating company, this election gave rise to a $2.1 million deferred tax asset and corresponding $1.5 million liability to converting shareholders on December 21, 2017, a $5.5 million deferred tax asset and corresponding $4.7 million liability to converting shareholders on December 22, 2016, a $6.1 million deferred tax asset and corresponding $5.2 million liability on May 12, 2016, and a $14.3 million deferred tax asset and a corresponding $12.2 million liability on July 27, 2015. The Company assessed the realizability of the deferred tax asset associated with the exchanges during the years ended 2016 and 2015 and determined that a portion of each of their benefits would go unutilized. Consequently, the Company established a $4.4 million, a $4.9 million, and a $11.0 million valuation allowance on December 22, 2016, May 12, 2016, and July 27, 2015, respectively, to reduce the deferred tax asset to amounts more-likely-than-not to be realized. These deferred tax assets remain available to the Company and can be used to reduce taxable income in future years. The Company similarly reduced the associated liability to selling and converting shareholders by $3.7 million, $4.1 million, and $9.4 million, at December 22, 2016, May 12, 2016, and July 27, 2015, respectively, to reflect

this change in the estimated realization of these assets. As required by the Income Taxes Topic of the FASB ASC, the Company recorded the effects of these transactions in equity.

After giving effect to the exchanges discussed earlier, as of December 31, 2016, the Company evaluated the need for the valuation allowance associated with the Section 754 tax elections as assets under management ("AUM") returned to pre-financial crisis levels, and brought revenue projections to a point at which the Company would generate sufficient taxable income to realize its deferred tax asset. Other positive evidence reviewed included: (i) the general positive economic environment, which has been reflected in stock markets and had a corresponding impact on AUM and revenue levels; (ii) performance records of almost all of the Company's strategies with 1, 3, and 5 year records that outperformed vs. their relevant benchmarks; (iii) the accelerating positive trends affecting the asset management industry in particular; (iv) the Company's history of positive operating and taxable income since 2007; and (v) the Company has no history of tax benefits expiring unused. These factors were moderated by negative evidence reviewed which included: (i) a high concentration of AUM in the three top client relationships; (ii) the difficulty of projecting AUM in the current volatile environment; (iii) market and competitive pressures in recent years that have created a trend towards lower management fees in the asset management industry; and (iv) the size and expected timing of Section 754 amortization and NOL carryovers.

As of December 31, 2016, the Company concluded that, after weighing both the positive and negative evidence, it was more-likely-than-not that it will generate sufficient taxable income in the future to realize its deferred tax asset. The reversal of the valuation allowance was based primarily upon the Company's sustained profitability in certain tax jurisdictions as well as projections of future assets under management levels. To reflect this change in the estimated realization of the asset and its liability for future payments, the Company increased its liability to selling and converting shareholders by $51.4 million for the year ended December 31, 2016. The effects of these changes to the deferred tax asset and liability to selling and converting shareholders were recorded as a component of the Income Tax Expense/ (Benefit) and Other Income/ (Expense), respectively, on the consolidated statements of operations for the year ended December 31, 2016. If evidence in future periods changes such that it is more-likely-than-not that part or all of the net deferred tax asset will not be realized, the Company will reestablish a valuation allowance at that time.

On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act into legislation. The Company has recorded a deferred tax expense of $26.5 million due to the re-measurement of the deferred tax assets due to a decrease in the federal corporate tax rate from 34% to 21% beginning in fiscal year 2018. The Company similarly reduced the associated liability to selling and converting shareholders by $20.8 million.

The Company identified an adjustment related to a change in the calculation of the 754 step-up in tax basis impacting the deferred tax assets and corresponding liability to selling and converting shareholders. As a result, the adjustment was made during the year-ended December 31, 2017, resulting in a $4.6 million decrease to the deferred tax assets and a $5.6 million decrease to the corresponding liability to selling and converting shareholders. The cumulative impact of the adjustment is a net tax benefit of $1.0 million which was recognized as a component of Income Tax Expense/(Benefit) in the consolidated statements of operations for the year-ended December 31, 2017 and did not affect the net cash provided by operating activities, net cash provided by/(used in) investing activities or net cash used in financing activities for the fiscal year ended December 31, 2017.

As of December 31, 2017 and 2016, the net values of all deferred tax assets were approximately $39.6 million and $73.4 million, respectively. These deferred tax assets primarily reflect the future tax benefits associated with the Company's initial public offering, and the subsequent and future exchanges by holders of Class B units of the operating company for shares of Class A common stock. At December 31, 2017 and 2016, the Company did not have a valuation allowance recorded against its deferred tax assets.

TABLE OF CONTENTS

Pzena Investment Management, Inc.

Notes to Consolidated Financial Statements (Continued)

Note 13 — Income Taxes (Continued)

The change in the Company's deferred tax assets, net of valuation allowance, for the year ended December 31, 2017, is summarized as follows:

	Section 754	Other	Valuation Allowance	Total
	(in thousands)			
Balance at December 31, 2016	$68,427	$5,014	$ —	$73,441
Impact of Tax Cuts and Jobs Act	(24,114)	(2,354)	—	(26,468)
Adoption of ASU 2016-09	—	1,377	—	1,377
Deferred Tax (Expense)	(5,139)	756	—	(4,383)
Unit Exchange	1,810	280	—	2,090
Impact of Change in Historical 754 Step-Up Calculations	(6,271)	1,669	—	(4,602)
Operating Loss Carryforward	—	(1,816)	—	(1,816)
Balance at December 31, 2017	$34,713	$4,926	$ —	$39,639

The change in the Company's deferred tax liabilities, which is included in other liabilities on the Company's consolidated statements of financial condition, for the year ended December 31, 2017, is summarized as follows:

	Total (in thousands)
Balance at December 31, 2016	$ (1)
Deferred Tax Expense	(1)
Balance at December 31, 2017	$ (2)

The change in the Company's deferred tax assets, net of valuation allowance, for the year ended December 31, 2016 is summarized as follows:

	Section 754	Other	Valuation Allowance	Total
	(in thousands)			
Balance at December 31, 2015	$64,877	$4,086	$(53,968)	$14,995
Deferred Tax (Expense)	(4,854)	1,284	—	(3,570)
Unit Exchange	11,605	—	(9,231)	2,374
Change in Valuation Allowance	—	—	61,942	61,942
Operating Loss Carryforward	—	(356)	—	(356)
Net Adjustment to Deferred Tax Asset[1]	(3,201)	—	1,257	(1,944)
Balance at December 31, 2016	$68,427	$5,014	$—	$73,441

1 During 2016, the Company recognized adjustments to the deferred tax asset and valuation allowance assessed against the deferred tax asset associated with a change in the effective tax rate.

The change in the Company's deferred tax liabilities for the year ended December 31, 2016 is summarized as follows:

	Total (in thousands)
Balance at December 31, 2015	$ (4)
Deferred Tax Expense	3
Balance at December 31, 2016	$ (1)

F-34

Pzena Investment Management, Inc.
Notes to Consolidated Financial Statements (Continued)
Note 13 — Income Taxes (Continued)

As of December 31, 2017 and 2016, the net values of the liability to selling and converting shareholders were approximately $36.4 million and $65.5 million, respectively. The change in the Company's liability to selling and converting shareholders for the years ended December 31, 2017 and 2016, is summarized as follows:

	For the Year Ended December 31,	
	2017	2016
	(in thousands)	
Beginning Balance	$65,485	$15,075
Impact of Tax Cuts and Jobs Act	(20,819)	—
Impact of Change in Historical 754 Step-Up Calculations	(5,608)	—
Release of the Valuation Allowance	—	51,442
Unit Exchanges	1,538	2,018
Tax Receivable Agreement Payments	(4,155)	(3,050)
Ending Balance	$36,441	$65,485

Note 14 — Quarterly Results of Operations (unaudited)

Unaudited quarterly results of operations for the years ended December 31, 2017 and 2016 are summarized below:

	For the Quarter Ended 2017			
	Dec. 31	Sept. 30	June 30	March 31
	(in thousands, except per share amounts) (unaudited)			
Total Revenue	$38,909	$36,229	$34,113	$32,044
Operating Income	20,934	18,404	16,619	13,097
Net Income	$(1,046)	$2,989	$2,629	$2,336
Basic Earnings Per Share	$(0.06)	$0.17	$0.15	$0.13
Diluted Earnings Per Share[1]	$(0.06)	$0.17	$0.15	$0.12

1 During the three months ended December 31, 2017, the calculation of diluted earnings per share resulted in an increase in earnings per share. Therefore, diluted earnings per share are assumed to be equal to basic earnings per share.

	For the Quarter Ended 2016			
	Dec. 31	Sept. 30	June 30	March 31
	(in thousands, except per share amounts) (unaudited)			
Total Revenue	$29,073	$26,990	$26,435	$25,838
Operating Income	13,709	11,952	11,261	10,296
Net Income	$10,986	$2,165	$1,406	$1,622
Basic Earnings Per Share	$0.67	$0.13	$0.09	$0.11
Diluted Earnings Per Share	$0.27	$0.12	$0.09	$0.10

Note 15 — Subsequent Events

The Company evaluated the need for disclosures and/or adjustments resulting from subsequent events through the date the financial statements were issued.

On February 6, 2018, the Company declared a year-end dividend of $0.42 per share of its Class A common stock which was paid on March 2, 2018 to holders of record on February 16, 2018.